

ERITREA



INTERIM
POVERTY REDUCTION STRATEGY PAPER
(I-PRSP)

Government of the State of Eritrea
Asmara, April 2004

ERITREA
INTERIM POVERTY REDUCTION STRATEGY PAPER (I-PRSP)
TABLE OF CONTENTS

	<u>Page Number</u>
ACCRONYMS	i
Country at a Glance	iv
Executive Summary	
I. INTRODUCTION	1
A. Background	1
B. Overview	2
C. Government's Commitment to Poverty Reduction	3
D. The Country and its People at a Glance	4
II. POVERTY IN ERITREA	
A. Incidence of Poverty	5
B. Data Sources on Poverty	5
C. Nature and Determinants of Poverty	9
D. Impact of Recent Events	11
E. Sources and Indicators of Vulnerability	12
F. Coping Mechanisms	13
G. Perception of the poor	14
III. DEVELOPMENT EXPERIENCE, MACRO ECONOMIC FRAMEWORK AND -SHORT AND -MEDIUM TERM PRIORITIES	16
A. Achievements and Developments During 1992- 2003	16
B. Accomplishments in Support of the Poor	17
C. War, Drought and Macroeconomic Imbalances	19
D. Medium –term Objectives and Priorities	22
E. Transitional Strategy to Recovery and Stabilization	23
F. The Macro Economic Framework 2004-2006	25
G. Mitigating Constraints to Growth and Stability	29
IV. INTERIM POVERTY REDUCTION STRATEGY	30
Pillar I: Reinvigorating Economic Growth	31

	Pillar II: Creating Income Generating Opportunities For the poor	38
	Pillar III: Improving Human Resources	42
	Pillar IV: Putting in place the Enabling Environment and Strengthening the Institutional Capacity	48
V.	PREPARATION AND CONSULTATION PROCESS	50
	A. Institutional Arrangement	50
	B. Consultation with Key Stakeholders	51
	C. Key messages that emerged from Consultations with Community Members and Representatives in the Regions	52
VI.	MONITORING AND EVALUATION	54
	BOXES:	
	Box 2:1 Stylised Figure on Poverty	7
	Box 2:2 Coping Mechanisms of the Poor	14
	Box 2:3 Peoples' Perceptions	15
	Box 3:1 The 2002/2003 Drought and its Impact	20
	Box 6: From I-PRSP to PRSP	58
	TABLES:	
	Table 2:1 Population below the Poverty Line in Eritrea	7
	Table 3:1 Key Macroeconomic Targets (2003-2006)	28
	Table 3:2 Leading Sources of Growth (2004-2006)	29
	ANNEX:	
	1. Time table for Processing PRSP	57
	2. Poverty Reduction Policy Matrix	59

Abbreviations and Acronyms

BoE	Bank of Eritrea
DANIDA	Danish International Development Assistance
DHS	Demographic and Health Survey
DRP	Demobilization and Reintegration Program
ECDF	Eritrean Community Development Fund
ECDP	Early Childhood Development Project
EFA	Education For All
EIA	Environmental Impact Assessment
EPLF	Eritrean Peoples Liberation Front
ERREC	Eritrean Relief and Rehabilitation Program
ERP	Emergency Recovery Program
EU	European Union
FAO	Food and Agriculture Organization
GER	Gross Enrollment Ratio
GoE	Government of Eritrea
GEF	Global Environmental Facility
HAMSET	HIV/AIDS, Malaria, Sexually Transmitted Diseases, and Tuberculosis
IC	Investment Center
IDA	International Development Association
IPRSP	Interim Poverty Reduction Strategy Paper
LSMS	Living Standards Measurement Survey
MDG	Millenium Development Goals
MoF	Ministry of Finance
MoFi	Ministry of Fisheries
MND	Ministry of National Development
MoLHW	Ministry of Labor and Human Welfare
MT	Metric Tonnes
NEMP	National Environmental Management Plan
NGO	Non-Governmental Organization
NORAD	Norwegian Agency for Development Cooperation
NSEO	National Statistics and Evaluation Office
PPA	Participatory Poverty Assessment
TA	Technical Assistance
UNDP	United Nations Development Program
UNMEE	United Nations Mission in Eritrea and Ethiopia

Eritrea

Interim Poverty Reduction Strategy

Country at a Glance

A. POPULATION AND SOCIAL INDICATORS

Population (million 2002) ¹	3.56
GDI per capita (USD) ²	190
Population growth rate (average annual growth %)	2.7
Poverty (% of population below poverty line) ³	66
Urban population (% of total population)	30
Life expectancy at birth (years)	52
Infant mortality (per 1,000 live births)	48
Child malnutrition (% of children under 5)	38
Access to an improved water source (% of population) ⁴	46
Illiteracy	44
Gross primary enrolment	57

B. KEY ECONOMIC RATIOS (2002)

GDP (US \$billion) ⁴	0.72
Gross domestic investment/ GDP	19.8
Export of goods and services/GDP	21
GDP (average annual growth)	3.1
GDP per capita (average annual growth)	2.5

C. STRUCTURE OF THE ECONOMY (% of GDP in 2002)

Agriculture	21
Industry	22
Services	58

¹ GoE, LSMS, National Statistics Office, 2003

² World Development Report, 2003

³ GoE, DHS, National Statistics Office, 2003

⁴ World Development Report, 2003

INTERIM POVERTY REDUCTION STRATEGY

I. INTRODUCTION

A. Background

1.1 This Interim Poverty Reduction Paper (I-PRSP) provides an overview of the nature of poverty in Eritrea and a statement of the Government's commitment to poverty reduction. It lays out the Government's macroeconomic framework and steps to create the conditions for resuming rapid economic growth, and policies and programs for poverty reduction. It presents an initial articulation of a national strategy that aims at directly impacting on poverty through broad based economic growth and targeted interventions. The strategy and the processes followed in its formulation are country-owned and reflect national priorities and local realities.

1.2 The process of I-PRSP preparation involved three interrelated steps. The first was carrying out a comprehensive poverty assessment. The second was drafting a poverty reduction strategy and the third was conducting consultations with key stakeholders (including with staff of sector ministries, provincial administrators, NGOs, private sector and community members in all the six Zobas. This document has benefited from valuable inputs from various sector ministries and comments from non-governmental organizations (NGOs), private sector, community groups and development partners.

1.3 The Government has also prepared a Food Security Strategy (FSS)¹ in-tandem with the I-PRSP -- both integral elements of the national development strategy. Preparing the two strategies simultaneously has the following advantages:

- (a) Builds critical linkages between the two strategies. Food insecurity is both a cause and consequence of poverty and by developing the two strategies simultaneously, critical linkages can be identified thus resulting in an overall impact greater than if each of the strategies were developed independently;
- (b) Exploits critical synergies between the two. Given the multi-layered nature of food security encompassing supply, access, affordability and vulnerability to shortages, food security is embedded in the government's strategies for poverty reduction and national development; and
- (c) Reduces duplication of efforts. Integrating these two strategies and linking them to the macro-economic growth strategy of the country will also help reduce duplication of efforts that could result in multiplicity of unconnected strategies, a critical concern for a country

such as Eritrea with limited institutional and human capacities and financial resources.

B. Overview

1.4 In addition to the Introduction in Chapter I, the I-PRSP contains five sections and three annexes:

- Chapter II - A Comprehensive Assessment of the poverty situation to gain a clear understanding of the extent, depth and distribution of poverty and the underlying causes and sources of vulnerability and the impact of the recent events (drought and border war) on the incidence of poverty;
- Chapter III - Eritrea's Development Experience, including achievements, during 1992-97, and developments during 1998-2003, focusing primarily on the impacts of the war, drought, and macroeconomic imbalances; immediate and Medium-Term development objectives, strategies and priorities for 2004-07; the Government's Macroeconomic Framework⁵, including the likely sources of growth and key targets for 2004-07; and concluding with a discussion of mitigating constraints to growth and stability;
- Chapter IV - Main elements of Eritrea's Interim Poverty Reduction Strategy built on four Pillars: (1) Reinvigorating economic growth; (2) Creating income earning opportunities for the poor; (3) Enhancing access to and utilization of essential services for human development; and (4) Promote active participation of the people in the political, economic and social aspects of nation building by putting in place an enabling environment and strengthening the institutional capacity. Attention is given to supporting policies and priority investment programs and institutional capability designed to directly assist the poor, including meeting targets and MDGs for selected national goals;
- Chapter V - A summary of the country-driven I-PRSP preparation and consultation process with various stakeholders (civil society, NGOs and development partners, and regional and national governments and community groups to ensure consensus on the overall focus and direction of the strategy and the programs for implementation reflect national priorities and local realities;
- Chapter VI - Mechanisms for monitoring and evaluating the strategy and the effectiveness of policies and programs in reducing poverty; developing intermediate indicators for timely monitoring of performance and

⁵ The Medium Term Development Framework (2004-06) [under preparation and expected to be completed by June, 2004]; The policy commitments and targets are tentative and will be revised later as more accurate data are made available and analysis done.

feedback (to complement measurements of poverty outcomes); identify and develop monitorable indicators for poverty reduction.

Annexes: I. Policy Matrix
II. Timetable for processing PRSP

C. Government's Commitment to Poverty Reduction

1.5 Poverty reduction and economic growth have been the central objectives of the Eritrean government since independence. The GoE has chosen a development strategy that promotes economic growth, and reduces poverty. The strategy involves four main elements.

- 1) Pro-poor economic growth strategy is essential for rapid poverty reduction
- 2) The development strategy promotes growth with equity that is broad-based so that the gains of growth accrue to the majority of the poor
- 3) Sound macroeconomic management and effective implementation of sector policies is essential for rapid economic growth and poverty reduction
- 4) Security is an essential pre-requisite for development including poverty reduction
 - This allows for a rationale on the continued focus on ensuring heightened mobilization
 - Or implementation of the decision of the Border Commission on boundary demarcation
 - Accordingly ensuring national sovereignty, territorial integrity, food security, livelihood security and protection against unforeseen calamities (including natural calamities such as flood and droughts) and economic shocks is a crucial pillar of the poverty reduction strategy

1.6 Poverty reduction is Eritrea's major challenge and is therefore, placed at the top of the development agenda. Poverty is seen as more than inadequate income or lack of human development; it encompasses managing vulnerability and encouraging popular participation to ensure inclusive growth. Gender equality constitutes a key element of the country's poverty reduction strategy. Eritrea's development strategy⁶ emphasizes people as the most valuable central resource that the country will depend for its reconstruction and development and this is reflected in the national theme "Our People are our Future".

1.7 The people of Eritrea displayed a strong capacity for organization, discipline, sacrifice and perseverance in winning the war of liberation and securing independence. They possess the same capacity to win the war against

⁶ The Government's economic growth and poverty reduction strategies are articulated in the Macro Policy Paper (1994), the 1991/94 Investment Codes, the National Economic Policy Framework and Program (1998) and the Transitional Economic Growth and Poverty Reduction Strategy (2001) and more recently in " A Framework for Medium-Term Development Plan", which is under preparation

poverty as well. The Government is committed to the objectives, the stated goals and targets of the I-PRSP. It is also committed to strive towards reaching the Millennium Development Goals (MDGs) on, among others, education, health, gender and poverty. Achieving these targets requires the mobilization of not only domestic efforts but also significantly larger injection of external financial resources.

D. Eritrea – the Country and its People at a Glance

1.8 Geography and History. Eritrea is strategically situated in the Horn of Africa serving as a bridge between the rest of Africa and the Middle East and the Gulf States. It covers an area of about 123,000 square km, roughly the size of England. Eritrea has a 1,200 km long coastline along the important Red Sea oil and shipping route connecting the Mediterranean Sea with the Indian Ocean.

1.9 The country exhibits a varied topography, rainfall and climate with altitude that ranges from 60 meters below sea level to over 3,000 meters above sea level. There are three major agro-climatic zones: the Western Lowlands, the Central and Northern Highlands, and the Eastern Lowlands (also referred to as the Coastal Plains). The temperature is generally cool in the highlands, where some 65 % of the population lives, while most of the western lowlands and coastal plains are for the most part hot and dry. The mean annual rainfall ranges from less than 300 mm in the coastal areas to a wider range from 400 mm to 1,000 mm in the highlands and the western lowlands. There are two major periods of precipitation in Eritrea: one from June to September, covering both the Western Lowlands and the Highlands and the second between October and March covering the Eastern Lowlands.

1.10 Society and Administrative Regions. Eritrea has a population of about 4 million people, of which about 3.6 million are resident. They are equally divided between Christians and Muslims. It is home to nine ethnic groups, each with its unique cultural heritage and language, while tied together with a strong sense of Eritrean national unity. Administratively the country is divided into six zobas (regions): Anseba, Debub, Debubawi Keih Bahri, Gash Barka, Maekel, and Semenawi Keih Bahri.

1.11 The Italians first claimed Eritrea as their colony in 1890. As the Allied Powers won the World War II, Italy lost Eritrea to the British, who set up a Military Administration and ruled the country from 1941 to 1952. In 1952, Eritrea was forcibly joined with Ethiopia through a United Nations imposed federal system of Government. In 1962, Ethiopia unilaterally nullified the Federal Act and annexed Eritrea as its province. The Eritreans peacefully protested this action and started the armed struggle for independence in the same year. After a protracted 30-year war with Ethiopia, Eritrea achieved its independence in 1991, and two years later it became formally an independent country.

1.12 At the time of independence, the new Eritrean Government inherited a devastated infrastructure, inefficient agricultural, manufacturing and service enterprises and weak public institutions. Like the rest of the economy, Eritrea's once growing and promising export sector was crippled. Exports were limited to basic commodities and consumer products that did not generate the foreign exchange needed to import machinery, equipment and production inputs. Jobs were scarce, and poverty was widespread among both the rural and urban residents. The private sector, which at one time was dynamic and dominant in the economy, was severely repressed. It had limited capacity to invest and lead economic recovery and lay the foundations for long-term growth and development.

II. POVERTY IN ERITREA

2.1 Eritrea is a poor country with an estimated annual GDP of about US\$ 180 per capita in 2002. At independence, the government concentrated on meeting the emergency needs of the people, rebuilding and rehabilitating its economic and social infrastructure and the institutions essential for achieving rapid economic and social development. The Government put in place a Macro Economic Policy Framework (para. 1.5) and made key investments in priority sectors to accelerate economic recovery and address the deep-rooted problems of poverty. By early 1993, Eritrea had managed to lay the basis for broad-based and sustainable growth. The economy registered a growth in GDP of about 7 percent over the period 1993-97 and much progress was made in increasing access to education and health facilities and rural roads with significant positive impact on the living conditions of the people.

2.2 The border conflict with Ethiopia during 1998-2000 disrupted Eritrea's initial progress, caused the destruction of economic and social infrastructure including roads, bridges, businesses, farms, schools, clinics and homes. It displaced over one million people, mainly farmers, the elderly, women and children. It also caused the disruption of economic activities and slowed down domestic and foreign direct investment, resulting in major macro-economic imbalances and stagnant or minimal growth of the economy. The situation was made worse by the onset of the worst drought in many years. The poor rainfall in several regions of the country resulted in crop failures that left over 60 percent of the population without adequate food.

A. Data Sources on Poverty

2.3 With a view to fully understand the degree and extent of the overall poverty situation in the country, the Government conducted a national household survey and formulated a strategy to address poverty in Eritrea. The Ministry of National Development (former Macro Policy, Office of the President) led the overall efforts. The following two surveys were completed in 2003:

- Household Living Standards Measurement Survey (LSMS). The National Statistics and Evaluation Office (NSEO) conducted this survey in 2003 with a view to fully understand the nature, extent and causes of poverty;⁷ and
- Participatory Poverty Assessment (PPA). The PPA provides qualitative information on the dimensions of poverty and valuable insights on the perceptions of the poor. An experienced team of Eritrean consultants conducted the participatory assessment that collected and analyzed data on poverty (for households and communities in selected villages in all Zobas).

2.4 Two complementary studies were also completed in 2003, namely:

- The Second Demographic and Health Survey (EDHS) also conducted by the NSEO in 2002, provides valuable information on the status of health, nutrition and demographic parameters in Eritrea, including estimates on fertility, mortality, family planning, maternal and child health, and nutrition for all six Zobas with a breakdown for urban and rural areas.
- The Rural Livelihood Security Assessment (2003)⁸ describes the food security situation of rural households throughout Eritrea, identified the most vulnerable geographic areas, and vulnerable households. The survey collected and analyzed data on household resources, livelihood strategies and availability of health services, access to water, etc.

2.5 On the basis of information collected and analyzed from the LSMS, complemented by the findings from the other three studies listed above, the NSEO carried out a comprehensive assessment of the poverty situation in Eritrea and produced a report: "Dimensions of Poverty in Eritrea".⁹ These four surveys have significantly increased our understanding of the nature, extent, geographical distribution, and structural causes of poverty. The results of these surveys provided a sound analytical basis for formulating the Interim Poverty Reduction Strategy. The priority policy and investment measures outlined in the draft strategy are aimed at addressing the underlying causes of poverty.

⁷ The first rapid poverty assessment was carried out in 1996 based on information from a survey conducted in 1993–94.

⁸ Eritrea: Rural Livelihood Security Assessment (July, 2003), ERREC, WFP and CARE Eritrea (July 2003). It established a baseline of indicators to monitor the impact of the drought on household food security

⁹ The Social Policy and Development Center (SPDC) in Pakistan provided technical support to the NSEO at the various stages of the household survey and preparation of the poverty assessment. The UNDP, UNFPA and WFP funded the various tasks related to the field survey, and report writing.

B. Incidence of Poverty¹⁰

2.6 According to the LSMS, 66 percent of Eritreans were unable to obtain sufficient food (in terms of calories) and other essential goods and services to lead a healthy life [Table 2.1]. Among these, approximately 37 percent live under extreme poverty, i.e., below the food poverty line. In rural areas, about 65 percent of the population is unable to obtain sufficient food (in terms of calorie intake) and other essential goods and services to lead a healthy life. In Asmara, the capital city, the incidence of poverty is about 56 percent and the incidence of poverty is higher in smaller urban centers. The proportion of the population that is poor and dependent on food assistance has increased because of the adverse effects of the recent border war and severe drought.

Table 2.1 Population Below the Poverty Line

POVERTY INCIDENCE (HEAD COUNT)			
Location	Population (%)	Poor (%)	Of which Extreme Poor (%)
Rural	68.8	64.64	38.90
Urban	31.2	70.32	32.65
Overall	100.0	66.40	36.97

Source: LSMS and Dimension of Poverty, NSEO, 2003

Note: The Poverty Line is Nakfa 240 per capita/month; Extreme Poverty line : Nakfa 150 per capita/month

2.7 An overview of the poverty situation in Eritrea reveals the following stylized facts below.

Box 2.1: Facts on Poverty in Eritrea

- The poor constitute about 66% of the population, (or 2.36 million), of which 37% are extreme poor--living below the food poverty threshold. About 67 percent of the poor live in rural areas of which about 39 percent are extreme poor.
- Poverty incidence shows significant variation among Zobas with the Northern Red Sea and Anseba having the highest poverty followed by the Southern Red Sea.
- Poverty is strongly related to lack of access to basic services such as education (especially literacy level of head of household) and health care and cultivable land.
- In rural areas, the poor households cultivate only 0.9 hectares of land, less than the average of 1.1 ha for each household; they are less able to diversify their agricultural production and are thus more susceptible to

¹⁰ A more detailed presentation of poverty indicators including definitions and methodology is presented in "Dimensions of Poverty (March, 2003)".

economic shocks.

- The poor, in particular the rural poor, have larger families (average of 6 persons) compared to only 4.2 persons for the non-poor. The average family size in Eritrea is 5.1 persons.
- About 30% of households are headed by women (of which 18% are widowed); on average female employees earn less than half that of males and a majority of the poor women in the rural areas are engaged in low-paying manual labor in construction and agriculture. Furthermore, female-headed households, have fewer household assets including livestock than male-headed households. Rural women are less likely to be literate and numerate - about 40% leave school at an early stage due to marriage. Rural women often do not receive antenatal care and suffer from poor nutrition.
- Urban poverty is more pronounced and serious than originally thought. About 33 percent of the country's poor live in urban areas, of which 11 percent reside in Asmara - the capital city; and 22% live in small towns.

2.8 Because the surveys were conducted during an abnormal year when Eritrea was hit by the worst drought since independence, the NSEO carried out a sensitivity test to assess the impact of the severe drought on the incidence of poverty and living conditions of the people. The analysis reveals that the overall poverty incidence would have been lower at 56 percent—a decrease of 10 percentage points under a scenario of normal weather conditions (average drought). Rural income decreased by about 18 percent due to the drought and urban purchasing power by about 10 percent, largely due to higher food prices that followed the severe drought.

2.9 Rural and Urban Dimensions. The challenges for the poor in rural and urban areas vary in nature and magnitude. The rural poor face a high risk because their income sources are not diversified they predominantly depend on rain fed agriculture, and face a high frequency of food insecurity. Physical infrastructure and access to social services are inadequate. Non-farm income is sought often through temporary/periodic migration. Rural residents face problems of access to land or insecurity in land tenure.

2.10 The urban poor earn income mainly from wage labor and informal sector activities including petty trade. The adequacy of food depends on cash availability. The physical and social infrastructure is of generally adequate quality and affordable for most residents. Housing is often costly or unavailable, thus forcing many to go to localities with poor or no water supply and sanitation facilities. Although they may be in close proximity to political power networks in the national capital as well as Zoba centers, the poor often have limited access to them. Therefore, they often rely on community and social networks which serve as important coping mechanisms.

C. Nature and Determinants of Poverty

2.11 Poverty is concentrated in rural areas, and is most severe in arid zones. About 67 percent of the poor live in rural areas and rely on low-input low-output agriculture and animal herding. The incidence and severity of poverty among rural inhabitants depend on the agricultural endowments of the region in which they live. Those living in chronically arid areas, such as the coastal plains and the northwestern lowlands are on average much worse off than those living in the wetter eastern escarpment, western escarpment, and central highlands (para. 1.8).

2.12 About 36 percent of the nation's people live in the arid areas. The great majority of them are semi-nomadic pastoralists who depend on cattle, camels, sheep and goats for food and income. During years of normal rainfall, they cultivate sorghum or millet, but during drought years, they sell their animals in exchange for grains and vegetables. Because they move frequently in search of water and grass for grazing animals, nomadic people are harder to reach with health care and education services. Consequently, they suffer higher rates of maternal, infant and child mortality and lower life expectancies than settled groups. They are also less likely to be literate, especially women.

2.13 The greatest number of poor live in the highlands. While poverty is more pervasive among people living in the arid regions, the greatest number of poor people live in the more densely populated highland regions. The majority of the highland poor possess a small plot of farmland of poor quality, rely primarily on subsistence agriculture (crop cultivation and animal husbandry) for their livelihoods. They have poor access to farm inputs (seeds, irrigation water and animal power), and show very limited engagement in non-farm activities, such as trade and remittances. This suggests that having opportunities for engaging in non-farm activities and receiving remittances from families and friends are critical for moving out of poverty.

2.14 Households headed by women are poorer than average. Approximately, 30 percent of the households are headed by women, of which 18 percent are widows -- the legacy of long year war of independence. Women comprise about thirty percent of the labor force indicative of a significant number that participate actively in the labor force. This group is, however, poorer on average than households headed by men because the majority of the poor women in the rural areas are engaged in low-paying manual labor in construction and agriculture and also because on average female employees earn less than half that of males. Furthermore, female-headed households have fewer household assets including livestock

2.15 Income is distributed unequally. The ratio of share of consumption by the richest quintile (top 20%) to that of the poorest quintile (bottom 20%) is 6.8, which is relatively high

2.16 The poor have limited access to social services. While much progress has been made in increasing access to basic social services since independence,

coverage and quality of social services is still poor in Eritrea. The poor not only have low levels of income and expenditure, but they also have more limited access to public infrastructure and basic social services including education, health, clean drinking water, and proper sanitation. Such limited access undermines their capabilities and severely limits their potential to secure gainful employment, and results in income poverty.

- Health and nutrition. In 2002, life expectancy at birth stood at 52 years, well below the average of 59 years for other low-income countries. Children suffer from malnutrition with about 38 percent under five years are stunted (low height for age), 15 percent are wasted (low weight for age) and 44 percent are underweight. Nearly 50 percent of children suffer from anemia. The maternal mortality rate is 250 deaths per 100,000 live births (facility-based) related mostly to complications during pregnancy and childbirth.
- Low access to education. At the time of the survey, about 28 percent of children aged 7-11 years were not attending school. The percentage of out-of-school children is 31 percent for girls and 25 percent for boys. In rural areas, about 45 percent of the children of the extreme poor were not attending school as they were engaged in various activities to support the family. Households that have the fewest number of individuals with primary education tend to be poorer. This demonstrates that education is critical to creating livelihood opportunities and diversifying income.
- Significant gap exists between rural and urban population. Households living in the highlands, and especially in the cities, are much more likely to visit health facilities and send their children to school than those living in rural areas. For example, Asmara, with 15 percent of the nation's population, has both the largest number and the highest quality of schools and health care facilities. The majority of women living in rural areas do not receive antenatal care at all. As a result, they have a high rate of maternal mortality, child mortality and child malnutrition in comparison with those living in urban areas. Similarly, school enrollment ratios are lower, and repetition and drop out rates higher in rural areas especially for girls.
- Inadequate access to potable water and sanitation. Approximately 18 percent of rural inhabitants have access to clean water from public taps.¹¹ The majority obtain their water supplies from streams or ponds during the rainy season and from deep wells at other times of the year. Women and children typically spend up to two hours a day fetching water, and more during the dry season. On the other hand, about 67 percent of urban residents have access to tapped clean water.

11 - Demographic and Health Survey, NSEO, 2002

Many poor urban dwellers live in peri-urban areas, which are not served with piped water supplies. They buy water from private vendors or municipality tanker trucks. Like the rural poor, they lack access to sanitation facilities.

2.17 The poor have larger families and a high dependency ratio. Family size is directly related to poverty status. The extreme poor have larger families (6.1), compared to the non-poor (4.2). The survey results show a strong positive relationship between dependency ratio and poverty.

2.18 Lack of asset ownership. The poor lack access to productive assets mainly farm land, and livestock. The value of assets owned and food consumption levels have strong positive relationship. Poor households also lack access to credit, because they have fewer assets to use as collateral and may have fewer social support networks.

D. Impact of Recent Events (war and drought) on Poverty

2.19 Border War. After six years of steady growth in the economy following independence, a border dispute with neighboring Ethiopia disrupted Eritrea's progress, caused the destruction of economic and social infrastructure, including schools and clinics, the disruption of economic activities, the displacement of nearly one million Eritreans residing especially in the agricultural areas of Gash-Barka and Debub Regions. In addition, large tracts of fertile land and pastures in the border areas remain inaccessible for farming due to land mines (Para 3.15-3.16).

2.20 Drought. The 2002 drought --the worst since independence in 1993, threatened the lives of over 1.4 million Eritreans, more than one-third of the population. An almost complete absence of rain seriously undermined agricultural production, even in the most fertile areas of the country. Crop production dropped sharply in 2002 to an estimated 54,000 metric tons (MT), only about one-fourth of the average production during the past ten years. Furthermore, drinking water became increasingly scarce, both for humans and livestock. A significant number of livestock died or were sold off by farmers to mitigate the adverse impacts of the drought. In 2003, although the amounts of kremti rains (June-September 2003) were about average in most areas of the country, long dry spells alternated with torrential downpours, impacting adversely on crop production, which was only about 106,000 MT. The drought also reduced the availability of seeds and affected the 2003-plantings. (box 3.1).

2.21 The border conflict and the drought resulted in major macroeconomic imbalances and stagnant or minimal growth in the economy. Refugees returning from Sudan and Eritrean's of Ethiopian origin that have been expelled from Ethiopia have come with few resources other than their know-how and willingness to work hard. These factors together are likely to add to the numbers of poor in Eritrea.

E. Sources and Indicators of Vulnerability

2.21 Sources of Vulnerability The main sources of vulnerability are external and internal shocks that include: (a) food insecurity (due to drought, pest infestation or military conflict); (b) single source of income and employment (agriculture-based source of livelihood is vulnerable to drought, pests, degradation of natural resources and fragmentation of small holder farms); (c) lack of access to and poor quality of basic social services and infrastructure (in particular water during drought conditions); (d) lack of access to productive assets (land, credit and farm equipment) and markets; and (e) lack of adequate social safety nets to protect the socially and economically vulnerable.

2.22 The survey results show that the most vulnerable are mainly-

- Households that live in high rainfall zones and depend on agriculture as their primary livelihood strategy. They are more food insecure because they are more dependent on fewer livelihood activities, particularly on subsistence agriculture. Communities situated in the lower rainfall zones appear to have a greater diversity of livelihood activities which allows them to spread their risks. They depend on livestock production as their main source of subsistence and livestock sales for weathering the crises and maintaining adequate levels of food consumption. They own animals that are more drought tolerant and therefore are less susceptible to climate variability.
- Households with the highest dependency ratios. They are highly vulnerable particularly those in the highest rainfall zones. Poor households are employing coping mechanisms that increase their long-term vulnerability. For example, the majority are consuming their planting seed stock and nearly half are selling off farm implements to respond to food scarcity;
- Female-headed households. They are more vulnerable than male-headed households. Gender could be seen as a source of vulnerability because of gender bias in employment and wages reflected in substantial differences in the level of income earned and the concentration of females in low-skilled and low-status jobs; and
- Socially and economically disadvantaged persons. These include children in difficult circumstances (e.g. orphans, street children), the disabled, commercial sex workers and socially disadvantaged persons (e.g. the destitute, displaced returnees and deportees, and the elderly).

F. COPING MECHANISMS

- 2.23 Eritrean communities have developed indigenous social welfare systems and ecological coping mechanisms that protect the poor from, hunger, starvation and death even under the most difficult circumstances.

Box 2.2 Coping Mechanisms of the Poor

A. Social Coping Mechanisms

- Alternative sources of income include: (i) fetching gold, sea products, forest products, using pack animals in and around the village, between the villages and market centers, (ii) plowing the fields of villagers who have neither plow animals nor labor to do the job; and (iii) collecting water or firewood and selling it in villages and towns
- Outside the traditional subsistence economy, coping mechanisms include seeking jobs in towns, and neighboring countries, selling the remaining productive assets to keep the family alive and selling jewelry that was given to the women of the households on the occasion of their marriage as a last resort.

B. Ecological Coping Mechanism

Three differing approaches are observed:

- The conservationists who have lived in the same environment for many generations have a deep knowledge of the natural vegetation and they tend to it with care - "if you know your trees, you will never starve." Knowledge of the trees whose leaves are edible, therefore, becomes important because such leaves are available year round and can compensate for the seasonally restricted availability of the green leafy vegetables
- The pioneers are those who moved away from their original habitat during the last generation or two and left their barren, degraded fields in the highlands to seek their fortune in the great river basins of the lower Mareb, the Gash, and the Barka rivers. They see their habitat as a "production site." Their motto is exploit the land, scoop off the wealth while you can, and when the land is denuded and exhausted move on to another site.
- The pastoralists have a highly protective attitude toward the riverine forests that give them fodder for their animals, supplementary food for humans, construction materials for their homes, and materials for their craft products. They have an adequate body of knowledge of trees and use it in times of drought and famine. However, they know a great deal more about animal fodder for their livestock than wild famine foods for humans.

- 2.24 When the normal agro-pastoral system of production faces difficulties, the community supports in rebuilding the herds of destitute families to the level at which they can be self supporting. Whereas the ecological coping mechanisms are ultimately vulnerable to climatic hazards, the social mechanisms can continue to function during periods of crises. They begin to decline only when the extent of poverty is so pervasive and so deep that the well-off members of the community also become impoverished and the traditional safety net system buckles under.

G. Perceptions of the Poor.

2.24 The PPA presents peoples' perceptions to rank their choices as individuals and communities regarding the causes of poverty and measures to alleviate poverty, as summarized in Box 2.3.

Box 2.3 Peoples' Perceptions

The priority measures for poverty alleviation for the individual and communities are ranked and summarized below.

A. Individual Perspective.

- Credit Purchases. Indigenous credit arrangements prevail in many rural communities in Eritrea. As drought intensifies, the poor families take food and other necessities on credit.
- Production Assets. Camels, goats, cattle and sheep (in declining order of importance) are the principal means of livelihood, particularly for pastorlists and are key coping mechanisms for resident farmers.
- Food Assistance when households do not have able-bodied members who can produce food or earn an income, or resources like pack animals that can generate income, or access to the traditional welfare institutions, or knowledge of wild famine foods, they have to rely on food aid provided by the state.
- Adequate Housing. The housing problem is severe in urban and peri-urban communities. The pace of urbanization has far outstripped the rate of home construction, particularly low cost housing that can serve the needs of the poor.

B. Community perspective

- Peace is at the top of the priority list. Nearly all the communities acknowledge the obligation of the young to defend their nation. The absence of the young labor force is their main concern. They propose partial demobilization as a way out of poverty, and their assumption is that their children will return to the villages and engage in farming, herding, and craft activities that they left behind.
- Access to Adequate Health Facilities is considered a key element in alleviating their poverty. Lack of good health is directly implicated in the impoverishment of households.
- Jobs/employment mainly in the form of cash for work programs to rehabilitate drought stricken population in the near term.
- Access to farm inputs, schools, drinking water supply, rural roads and micro credit schemes (in declining order of importance).

III. DEVELOPMENT EXPERIENCE, MACROECONOMIC FRAMEWORK AND SHORT- AND MEDIUM-TERM PRIORITIES

3.1 This Chapter summarizes Eritrea's development experience since independence, focusing on achievements during 1992-2003 and the setbacks caused by the border war with Ethiopia as well as the string of severe droughts during the period. It also outlines the main challenges facing Eritrea and the

Government's strategies, priority policy measures during the transition and in the medium-term aimed at directly impacting on poverty.

A. Achievements and Developments, 1992- 2002

3.2 Having inherited a ruined economy at independence, the new Eritrean Government pursued policies, strategies and investment programs to promote rapid and sustainable growth. The role of the government was limited mainly to creating an enabling environment and investing in rehabilitation and expansion of critical infrastructure, including roads, and health and education facilities.

3.3 From independence until the eruption of the border war in 1998, the government implemented several critical measures that guided and facilitated the restructuring and growth of the economy. The main features were:

- Reforming the civil service, reducing the public sector workforce by 30 percent, introducing an incentive-based remuneration system, and redeploying personnel to offices in the administrative regions;
- Restructuring government ministries, refocusing their main functions on formulating national policies and regulations, research, and development of human resources, while delegating responsibility for implementation to regional/local governments;
- Demobilizing and reintegrating over 55,000 former combatants into private civilian life, providing support to the families of up to 34,000 martyred and about 10,000 disabled combatants, and resettling over 190,000 returning refugees;
- Reforming the tax system and its administration, reducing tax rates for most payers, broadening the tax-base, reducing tariff rates on imports, upgrading staff skills and computerizing tax administration.
- Facilitating private sector development by establishing a one-stop business licensing office that significantly reduced the time needed to obtain licenses; privatizing public enterprises through open competitive bidding; and enacting a new land proclamation to ease investor access to land;
- Adopting legal frameworks for the operations of Eritrea's new Central Bank --the Bank of Eritrea, and for the financial institutions and legal measures that facilitated the introduction of the new Eritrean currency, the 'Nakfa', unifying the two-tiered exchange rate, and broadening the foreign exchange market by licensing foreign exchange bureaus; and

- Putting in place broad-based fiscal, monetary, and trade policy regimes aimed at mobilizing government revenues, facilitating efficient allocation and utilization of resources, and maintaining macroeconomic stability.

3.4 These reforms had a positive impact on macroeconomic performance. The fiscal deficit (including grants), which had increased sharply to 25 percent of GNP in 1995, declined to 21 percent in 1996 and to 5 percent in 1997. The decline in the fiscal deficit reflected reductions in one-time outlays associated with demobilization of ex-combatants, support for families of martyred and disabled combatants, and costs associated with reducing the civil service. To further contain inflationary pressures, increases in capital expenditures were also moderated. Moreover, tax revenues rose sharply, from 13.6 percent of GDP in 1992 to 18.5 percent in 1997. Inflation declined from about 13 percent in 1995 to about 4 percent in 1996 and to about 2 percent in 1997 as the government cut spending to build up international reserves to prepare for the introduction of the Nakfa.

3.5 The newly introduced currency, the Nakfa was stable and backed by gross foreign exchange reserves that covered over five months of imports of goods and services; the external current account, including official transfers, was in balance, despite record imports, financed mostly by large private transfers of the Eritrean Diaspora; public debt, which was non-existent at the time of independence, remained insignificant.

3.6 By early 1998, most of the transition issues had been successfully addressed, investor confidence was beginning to grow and private investment in a number of sectors was increasing, and the economy was growing rapidly.

B. Accomplishments in Support of the Poor 1992-2002

3.7 From 1993 through 1997, significant progress was made toward achieving macroeconomic stability. The basis for sustainable broad-based growth was laid whereby most of the transition issues were addressed successfully, and private entrepreneurs responded to opportunities by investing in the services, construction and other sectors, which led the early growth of the Eritrean economy resulting in increased opportunities for employment and better livelihoods for low income households including women. The main accomplishments are summarized below.

3.8 Education. Access to education increased at elementary, middle and secondary school levels. In 2001, academic year enrollment in elementary education increased by 62 percent as compared to 1992, while in middle and secondary education, it increased by about three and two fold respectively. The enrollment of girls in government schools increased by about 78 percent for the same time period while enrollment in adult literacy programs increased by about 11 percent. The number of government schools increased by 70 percent in

elementary, more than two fold in middle, 85 percent in secondary, and more than three fold in technical schools. Similarly the number of teachers increased by about 44 percent. As of 2001, there are 579 elementary, 120 middle, and 37 public secondary schools, seven technical schools and one university. In addition there are 88 Elementary, 22 Middle, 6 Secondary and 3 Technical non government schools run by private sector, religious organizations etc.

3.9 Health. Access to health care services increased through restoration of health facilities damaged during the war, the construction of new facilities and the training of qualified health personnel. Health services in Eritrea focused on Primary Health Care (PHC) with emphasis on development of basic health services at the local level, with emphasis on preventive public health activities including the prevention and control of endemic diseases such as HIV/AIDS and other sexually transmitted diseases (STDs), malaria and tuberculosis. One notable achievement of Eritrea's health system has been the reduction in infant and child mortality. Infant mortality declined from 72 per 1,000 live births in 1992 to 48 in 2001. Mortality of children under five years declined from 140 per 1,000 live births in 1992 to 93 in 2001. (EDHS 2002) Considerable progress has also been made in bringing primary school education to the citizens of Eritrea. At independence, only about 58 percent of men and 28 percent of women could read and write. By 2001, 67 percent of men and 39 percent of women were literate.

3.10 Social Safety Nets. With the limited resources available in the early years of independence, the Government successfully reintegrated 55,000 combatants into civilian life; resettled about 190,000 returning refugees; and helped to take care the families of the tens of thousands of fighters who had died or were disabled during the war of independence. In addition, the government distributed food supply to the most needy who lived in drought prone regions.

3.11 Agriculture. Agricultural sector development has been hampered by recurrent droughts and the long war for liberation. In the Initial Phase (1993-1995) the focus was on increasing crop yields in traditional agriculture, construction of rural roads, bridges and earth dams and marketing centers, and strengthening the planning, programming capacity and research and extension capacity of the MoA. During the period 1996-2003, efforts were made to introduce modern farming practices through the integrated farming program, vaccinating livestock against major diseases, as well as training of farmers. The overall effort has produced good results, except in rainfed agriculture largely due to the recurring droughts.

3.12 Industrial Development. Early on, the Government adopted a two pronged strategy to develop its industrial base, namely development of labor intensive manufactured exports and development of the natural resource base to ensure supply of raw materials for industries in which the country has a comparative advantage. All sectors of the economy were opened up to private investment and almost all public enterprises were privatized. An investment policy that encourages foreign investment in all sectors of the economy was also

adopted. Developing a sound financial system, simplifying the tax structure and reducing the number of income tax rates were undertaken. Rehabilitating and developing the physical infrastructure including the ports of Assab and Massawa, water, electricity, transport and telecommunication facilities was carried out. Monetary policy was used to attract investments, stabilize prices and contain inflation.

3.13 Service Sector. This sector, made up of transport, communications, postal services, financial and business services, retail and wholesale trade, education, health and tourism, is a major source of employment. The enabling investment environment facilitated the growth of the service sector to account for about 50% of GDP in 1999.

3.14 Infrastructure. As of 2002 the country had a total of about 7,000 kilometers of road network (primary, secondary and feeder) for an average of 70 km. of road network per thousand square kilometers. In telecommunications, as of 2001 there were about 33,000 main fixed telephone lines compared to about 14, 000 in 1995. Overall government expenditures on infrastructure (ports, rail and communications, roads and water supply) increased to 344.3 million Nakfa or 13% of total government expenditure for that period.

C. War, Drought, and Macroeconomic Imbalances (1998 – 2003)

3.15 Border War. The border war with Ethiopia during 1998-2000 resulted in displacement of more than 1 million innocent Eritrean civilians residing mostly in Gash-Barka and Dehub Regions. Towns and villages were totally destroyed, thousands of livestock were killed, schools and clinics were wrecked, homes and farms and other productive assets and wealth were burned by Ethiopian troops, and basic infrastructure including water supply systems and roads were destroyed. The most vulnerable among the internally war displaced were children, women and the elderly. To meet the challenges of the emergency situation, the Government reallocated funds from its development budget for the importation of food, provision of emergency shelter, medicine and health care services, water supply and sanitation, and social and administrative services.

3.16 The Emergency Reconstruction Program (ERP) financed with the support of development partners, rehabilitated key roads and bridges in order to secure the timely delivery of food aid and social services to the war affected population, facilitate resettlement, and help reduce economic impacts by reducing transportation costs. The program financed construction of 64 sub- projects in health and education facilities, feeder roads, market centers, and water supply schemes. Furthermore, the ERP extended credit services to poor individuals and households in rural and peri-urban communities that do not have access to formal financial institutions, thus creating opportunities for income and employment through access to working capital. The program also expanded social infrastructure to hitherto underserved communities in Gash-Barka and

Debut to assist them in maintaining valuable social services and served as a source of employment in the communities involved.

3.17 Recurring Drought. During the period 1998-2003, Eritrea also suffered its worst drought in many years. The scant and erratic rainfall in several regions of the country resulted in widespread crop failures that left over 60 percent of the population without adequate food supplies (Box 3.1).

Box 3.1: The 2002/2003 Drought and its Impact

Causes. The current drought is the worst since the independence of Eritrea in 1991. An almost complete absence of rain has seriously undermined agricultural production, even in the most fertile areas of the country. The crisis has been aggravated by the continued mobilization of a large number of able-bodied farmers into the armed forces. In addition, sections of the most fertile land remain covered with mines from the 1998-2000-border war.

Impact. Crop production dropped sharply in 2002 with harvest estimated at about 55,000 metric tons (MT), equivalent to only 25 percent of the average production over the past ten years. In almost all the drought-affected areas, the ground and surface waters have been depleted. In the coastal areas, the water level has dropped by up to 10 meters. Furthermore, drinking water has become increasingly scarce, and considerable portions of the livestock have died. The drought threatened the lives of over 1.4 million Eritreans (more than one-third of the population). In addition, the large number of internally displaced people from the war, who are presently living in refugee camps, needed food and other humanitarian assistance.

The 2002 drought also reduced the availability of seeds and adversely affected the 2003 plantings. A significant number of livestock were sold off by farmers to mitigate the adverse impacts of the drought. Livestock represents the main mechanism utilized by farmers as a coping device against emergency.

In 2003, crop production was severely constrained by erratic rains starting late and ending early. Although the amounts of kremti rains (June-September 2003) were about average for most areas of the country, long dry spells alternated with torrential downpours, thus crop production for 2003 was about 106,000 MT. This drought condition has led to crop failures, loss of livestock and acute shortage of drinking water in some areas, thus exacerbating the already critical food and water shortages from last year's drought.

Immediate response. In November 2003, the government appealed for emergency food assistance, supported by the UN Consolidated Inter-Agency Appeal. The cereal import requirement for 2004 has been estimated at about 480,000(metric tones) Mt, setting the estimated domestic availability of 136,000 Mt against the estimated total utilization of approximately 600,000 Mt. Given

the precarious foreign exchange situation, it is anticipated that around 30,000 Mt of cereals can be commercially imported for consumption. With about 30,000 Mt of cereals in stock or in pipeline as food aid, the uncovered cereal deficit – for which international assistance is needed amounts to about 420,000 Mt.

Government Plans. To avert a humanitarian crisis in the face of inadequate and slow response from humanitarian agencies, the government was compelled to use much needed foreign exchange reserves to procure food from the international market. The 2004 budget provides for Nakfa 105 million in contingency funding for emergencies (amounting to about 30,000 tones depending on the exchange rate and food prices). Additional funds may be mobilized by cuts in other budgeted expenditures. However, the low level of foreign reserves limits the use of such funds for purchases from abroad. As a last resort, the Government stands ready to borrow abroad, preferably on concessionary terms, to avoid starvation of the population in 2004. Eritrean nationals in the country and abroad have made significant contributions towards meeting the challenge in year 2003, and it is hoped that they would rise to the occasion again in 2004.

The food security objectives are also expected to benefit from demobilization and demining. Over the next year, more than 120,000 persons are expected to be demobilized, many of whom will return to agriculture. The increase in arable land as a result of demining and the newly resettled areas by returnees from Sudan will also boost production

Tackling chronic food insecurity. The Government is working on a medium-term food security strategy to tackle the country's chronic food deficit. The strategy covers both national and household food security (para 4.4-4.48 in Chapter IV). The priority measures include, inter alia, strengthening water catchments and irrigation systems, enhancing the productivity of rain-fed agriculture, and increasing livestock and fish production and creating alternative sources of employment and income.

3.18 Macroeconomic Imbalance (1998-2003). The border war disrupted Eritrea's initial promising growth and reversed many of the macroeconomic gains. The invasion by Ethiopia caused the destruction of economic and social infrastructure, the displacement of more than one million people and the associated costs of relocation and resettlement. Furthermore, at the height of the conflict, agricultural, industrial, and commercial activities were disrupted with consequent slowdown in domestic and foreign direct investment; all resulting in major macro-economic imbalances and stagnation or growth in the economy. (see Table 3.1 below)

Table 3.1 Key Macroeconomic Indicators (1998-2002)

Indicators	1998	1999	2000	2001	2002*
------------	------	------	------	------	-------

GDP growth (%)	4.0	0.3	-12.0	9.0	-0.04
Inflation, (%)	16.6	8.2	20.8	13.5	15
Budget deficit (% GDP incl. Grants)	33.6	52.2	43.4	38.1	29
Reserves (months)	5	2	2	1	1
External public debt (% GDP)	18	37	50	60	77
Domestic public debt (% GDP)	56	90	123	104	120

* Estimates

Source: Government of Eritrea, Bank of Eritrea

3.19 During the past three years, the slow peace process diverted in part our attention and resources from development to consolidation of security. Now the Government has articulated its macroeconomic adjustment and development strategy and priorities, taking into account the enormous damage caused by the war. Through the Warsai-Yekealo campaign, all segments of the population are engaged in the rehabilitation and reconstruction of infrastructure necessary as a precondition for further investment and development. The overall development strategy of the Government is clearly stated in the Transitional Economic Growth and Poverty Reduction Strategy (TEGPRS) - 2001-02, and the Medium-term Economic Development Framework (MTDF), the Poverty Reduction Strategy (iPRSP) and the Food Security Strategy (FSS) that are currently being elaborated.

D. Medium-term Objectives and Priorities(2004-06)

3.20 Overall Objectives, Strategies and Policies. The longer-term objective is to attain rapid and widely shared economic growth with macroeconomic stability and a steady and sustainable reduction in poverty. The cornerstone of Eritrea's development strategy is investment in its human resources, technology, and economic infrastructure to enhance productivity, competitiveness in trade and investment in sectors in which Eritrea has a comparative advantage. While Government has a particular responsibility for spreading action and creating the enabling environment and macroeconomic framework, the private sector, non-governmental and community based organizations all have a vital role to play in meeting the challenges of poverty reduction.

3.21 The transitional medium-term (2004-06) objectives are to be pursued to promote economic growth and development. They include: (i) developing exports, (ii) increasing agricultural productivity, (iii) attracting investment in high potential growth centers mainly in fisheries, tourism, construction, manufacturing and regional trade, (iv) developing a strong financial sector, and (v) expanding and modernizing the country's basic infrastructure.

3.22 Eritrea's transitional growth and macroeconomic adjustment targets are summarized in Table 3.2. To achieve these targets and the objectives outlined in the preceding paragraph, the 2004 budget consistent with the MTFDF proposes a number of measures which can be grouped under four headings, namely: macroeconomic stabilization; enhancing human resource development; private sector development by creating conducive and business friendly environment that fosters competition; and developing critical economic infrastructure to enhance productivity, export competitiveness and trade.

3.23 Addressing the impact of the severe drought and major macroeconomic imbalances (fiscal, monetary and foreign exchange constraints), while at the same time restoring the development momentum are significant challenges. It will require a carefully thought out, properly timed, and coordinated set of actions through the 2004 budget in the context of the MTFDF. The Government is using the budget as one of the instruments to correct the prevailing imbalances and to restore macroeconomic stability. Accordingly, the budget for 2004 represents a major step toward achieving macroeconomic stability and fiscal and external account sustainability. The implementation of the budget and the adherence to MTFDF goals are expected to restore fiscal balance and investor confidence over-time, as well as contribute to the restoration of macroeconomic stability.

3.24 To obtain these transitional targets, we will begin immediately to implement rigorously a process of prioritizing, planning and budgeting, and introduce a more effective mechanism of coordinating, monitoring and evaluating programs and projects. We will strengthen public sector financial management by adhering to budgetary discipline, sound planning and budgeting. To mitigate the potentially negative effects of the adjustment program on poverty, we will carefully monitor the impact while concurrently developing appropriate food security and poverty alleviation strategies that will constitute integral parts of the MTFDF.

E. Transitional Strategy to Recovery and Stabilization

3.25 The transitional strategy for the short-term aims at addressing the more pressing problems before shifting full attention and resources to tackle the mainstream and mid-term development challenges. Toward this end, the Government considers the years 2004 - 2006 as a transition period during which the emergency and critical economic and social challenges would be tackled as a matter of priority, while important steps would also be taken to restore the development momentum and create the conditions for sustainable economic growth.

3.26 Immediate Priorities. During the transition period, Eritrea's immediate development priorities are:

- Meeting the Basic Needs of the Population. At a time when we had started to move away from humanitarian relief toward rehabilitation and recovery, we were faced again with the impact of severe droughts in 2002 and 2003. The droughts resulted in substantial crop failure. The population considered now vulnerable has reached an estimated two-thirds of the national population. The strategy is to meet the needs of the vulnerable population by further mobilizing funds from Eritrean nationals in and outside the country, government budgetary allocation and assistance from the international community.
- Achieving Macroeconomic Stability. The Eritrean economy is beset by severe macroeconomic imbalances epitomized by an unusually high level fiscal deficit. Reducing aggregate fiscal deficit substantially and over a relatively short period of time and invigorating the private sector are key to restoring macroeconomic stability. In 2002 budget deficit (including grants) reached a high of 29 percent of GDP and declining to an estimated 25 percent in 2003. Although the deficit has been restrained somewhat, the Government aims to further reduce the deficit through a drastic reduction in defense expenditures. The reduction in defense expenditures is predicated upon the demobilization of approximately 120,000 soldiers by the end of 2004, no increase of the size of the civil service in 2004. Furthermore, civil service pay that has been frozen since 1997, would be increased in 2004 only if the financial situation of the country improves significantly. The locally financed portion of capital expenditures will be limited to basic services and on-going high priority infrastructure and human development projects, and the proposed austerity budget for 2004 reflects these. In 2003, as a first step to reduce the large budget deficit, contain inflation, and restrain the further depreciation of the currency, the Government adopted an austerity budget. This has to be repeated in 2004.
- Managing the Public Debt. In the short period of five years since the start of the border war, both domestic public debt and external public debt have reached unsustainable levels. The growth of public debt, however, must be reined-in heavily. To this end, the Government intends to maximize mobilization of external assistance in the form of grants or a hybrid of grants and loans on concessionary terms. The growth of domestic public debt will be curtailed to a rate that is consistent with low inflation and a level that would not result in crowding out the private sector in the credit market.
- Rehabilitating and Expanding Infrastructure. We will continue investing in critical social and economic infrastructure including

water supply, rural roads, access to education, health-care and housing and rural electrification, with the limits of budget constraint.

- Resettlement and Reintegration. We will carefully plan and reintegrate IDPs, expellees, returnees and demobilized soldiers into normal and productive life in communities. Significant demobilization will substantially reduce defense expenditures and reinvigorate the economy by releasing a large pool of labor, both skilled and unskilled, to private and public sectors.

F. The Macro-economic Framework 2004-06

3.27 The Government of Eritrea is committed to pursuing fiscal, monetary, trade and investment policies that mobilize and allocate resources efficiently to achieve rapid economic recovery and development. These policies focus on maintaining macroeconomic stability and promoting competitive private sector development supported by effective public sector management. A summary of the most important aspects of Eritrea's economic policy framework is given below.

Fiscal policy

3.28 Tax and Revenue Policy. A tax structure that substantially improves mobilization of revenues, (promotes efficient use of resources), provides incentives to investors and achieves greater equity has been established. At the same time, personal and business income taxes and the sales tax structure have been simplified and streamlined, the number and level of customs duties have been reduced, and excise and sales taxes on luxury items have been increased to ensure that tax reforms are equitable and revenue neutral. The number of income tax rates have been reduced to five from eight and a top rate of 30 percent introduced in place of the current 38 percent. The five corporate tax rates have been replaced by a flat 30 percent and the special rate on reinvested profits has been eliminated. These and other measures including the removal of the sur-tax on personal income that was levied during the border conflict are expected to increase tax revenues moderately relative to GDP in 2004. To mitigate the cascading effects of taxation of intermediate inputs on the cost of domestic products, the tax rates applied on capital goods, intermediate inputs and raw materials have been reduced to a minimum. To promote international competitiveness, domestic producers are given only modest effective protection, if any.

3.29 As part of these improvements, the Internal Revenue and Customs Departments are now equipped with a large database to enhance effectiveness in tax assessment. Further strengthening of income tax collection has been instituted through improved record keeping requirements, strengthened audit capacity at the Inland Revenue Department (IRD) and Customs Department (CD) and adoption of self-assessment as the preferred method. The Government's efforts to improve tax and customs administrations have been reasonably successful.

3.30 Expenditure Policy. The sharp increase in current expenditure and budget deficits during the past four years are unsustainable and, therefore, harmful to the economy (para. 3.22). The Government is using the expenditure cutting option in the budget as one of the instruments to reduce the fiscal deficit and restore macroeconomic stability. This is being done with care to minimize the negative impact of reduced government expenditure on GDP growth and programs that directly impact on the poor. Accordingly, the Government adopted an austerity budget for fiscal years 2003 and 2004. If the projections are realized, the budget deficit would decline from 29 percent of GDP in 2002 to about 15 percent in 2004. This would contribute significantly to fiscal sustainability and macroeconomic stability.

3.31 While diplomatic efforts are underway to compel Ethiopia to implement the decision of the Boundary Commission on the common borders, the government is committed to implement a phased demobilization. This is expected to have a short-term negative impact on the fiscal side to cover financial assistance for basic needs and to help reintegrate those being demobilized into the economy and the society at large. In the medium-term, however, such curtailment of military expenditure will provide fiscal space for developmental and social expenditures and reinvigorate growth by making a large pool of skilled and unskilled labor available to the economy.

3.32 The government will also take further steps to underpin fiscal adjustment by increasing revenues from sale of public properties (mainly real estate in Asmara and Massawa and public enterprises), strengthening public sector financial management and adhering to budgetary discipline and control. To increase efficiency in resource utilization at all levels of government, action will be taken immediately to implement a more rigorous process of prioritizing, planning, monitoring and evaluation of projects.

Monetary and Exchange Rate Policies

3.33 The monetary and foreign exchange challenges that Eritrea faces are significant and redressing them will require a carefully thought out, properly timed, and coordinated set of actions. The Bank of Eritrea will pursue the following policies:

3.34 Credit and interest rate policies. The Bank of Eritrea (BoE) will use its monetary policy instruments to maintain price stability while influencing credit and interest rates to promote economic growth. It will adhere strictly to the prudent guidelines set by the Proclamation. The principal objective of the Bank shall be to manage money and credit in the Eritrean Economy, with the purpose of safeguarding the value of the national currency. According to the Proclamation, in pursuance of its monetary policy, the Bank of Eritrea shall

influence the supply of money, and credit, and may issue regulations with respect to the level of interest and Foreign Exchange rates. The restraint on expanding the monetary base and the restriction on provision of credit to the government are expected to reduce the inflationary pressure (para. 3.39).

3.35 Exchange Rates. The reform agenda includes a framework for establishing a more flexible exchange rate system that will gradually lead to the official exchange rate adjusting to the market rate. It should also lead to the establishment of an auction mechanism for allocation of official reserves. Such a system would be like the "managed float" system that the BoE had envisaged before the war broke out. However, to contain domestically and externally generated inflation, the move toward such a system should be accompanied by a tight monetary policy.

3.36 Current Account. The current account is projected to improve with reserves increasing from 1-2 months of imports equivalent in 2004 to 2 and 3 months during 2005 and 2006, respectively. Exports of goods are expected to increase during the same period. However, they will lag behind imports. Imports are expected to grow at a modest pace due to a substantial cut in defense-related imports, and a likely increase in importation for other uses, including food items.

3.37 Debt Management. As part of the determination to reduce the debt burden, the following actions are being taken: (i) reducing domestic borrowing from banks and financial institutions, (ii) relying to a minimum on external borrowing, except as a means of last resort, (iii) contracting of new external debt only on IDA or better terms, and (iv) seeking grant assistance to the fullest extent possible. External financing sources on favorable terms will also be sought. These include credits, often on concessionary terms, and grants from multilateral and bilateral sources, commercial loans on favorable terms to finance projects with high and quick returns, and investment by Eritreans in the Diaspora, which could become an important source of revenue and balance of payments support.

Trade and Investment Policies

3.38 Trade Policy. Eritrea is committed to maintaining an open and liberal trading policy and promoting regional economic cooperation. To encourage rapid expansion of trade and allow free mobility of capital and labor, the government has eliminated or substantially reduced all trade barriers, removed nearly all quantitative restrictions and prohibitions on imports, and the number of import tariff rates and the maximum have been lowered substantially. Customs administration has been streamlined by reducing and simplifying the steps and procedures required of importers before they obtain clearance. As for exporters, procedures have been simplified and all taxes have been eliminated.

3.39 In addition to these unilateral steps that have been taken or are being taken, Eritrea is working with countries in eastern and southern Africa to enhance free movement of goods and services in the region. Eritrea is a member

of both the Intergovernmental Authority on Development (IGAD) and the Common Market for Eastern and Southern Africa (COMESA), and is actively working for the elimination of trade barriers.

3.40 Investment Policy. Consistent with its strategy to develop an outward looking, private sector-led market economy, Eritrea has adopted very liberal investment policies. The economy has been fully open to private participation since 1994, when the government issued its investment and macro-policy documents (para. 1.4). The government views foreign investment and collaboration as an important means to supplement the country's limited supply of production technology, capital, and management and marketing skills. Therefore, foreign investment is encouraged in all sectors without restrictions related to ownership or capital structure. Foreign investors are treated the same as domestic investors in obtaining access to land, utilities and other production inputs. There are no exchange controls limiting foreign investors from repatriating their profits and capital gains through the domestic foreign exchange market. Foreign investors are allowed to bring in needed capital and production inputs upon payment of a minimal customs duty. Employment of expatriate staff whose skills are in short supply in the Eritrean market is also allowed, with clearance from the relevant authorities.

3.41 Macroeconomic Targets. During 2004-2006, the Government will strive to achieve the macro-economic targets summarized in Table 3.2 below.

Table 3.2. Macroeconomic Targets for 2004 – 2006

Major Indicators	2003*	2004	2005	2006
GDP growth (%)	5	8	8	8
Budget deficit (as % of GDP)	25	20	15	10
Inflation (% average)	18	15	10	5
Free Reserves (months of imports equivalent)	1	1.5	2	3
Budget Deficit (% of GDP including Grants)	25	20	15	10

* Estimates

3.42 During the period 2004–2006, real GDP is projected to grow by an average of 8 percent [Table 3.2]. This is based on the belief that crop production in 2004 will reach at least the 1999 production level, and that there will be a strong growth in the rest of the economy. The fiscal deficit (including grants) is expected to fall from 25 percent of GDP in 2003 to 20, 15, and 10 percent in 2004, 2005, and 2006, respectively. This is to be achieved mainly through a combination of a sharp reduction in defense outlays, the control of non-defense outlays, and projected increases in revenue owing to tax reform and improvements in tax administration. Another key macroeconomic objective is to reduce inflation from an estimated 18 percent in 2003 to 15 percent in 2004, 10 percent in 2005 and 5 percent in 2006. The most important restraint will come

from the stringent lending policy to government and the austerity budget that has been adopted.

3.43 Projected Sector Growth: Construction, fisheries, tourism, and agriculture are expected to be the lead growth sectors during 2004-2006 (Table 3.3 below). The construction industry is expected to be the single most important source of growth. There is a strong public-private partnership underway particularly in the construction of roads and highways, airports and ports as well residential housing, particularly low cost housing. The possibility of another severe drought notwithstanding, agriculture too is expected to register improvements while services; internal trade, fisheries and tourism will experience steady growth.

Table 3.3 Annual Sectoral Growth, 2004-2006 (projections)

Sector	2003	2004*	2005*	2006*
Agriculture	15	10	10	10
Fisheries	10	15	15	15
Industry	7	8	8	8
Tourism	5	10	10	10
Construction	10	10	10	10
Services	7	7	7	7

* Government projections
figures for 2003 are estimates

G. Mitigating Constraints to Growth and Stability

3.44 For the Eritrean economy to achieve continuous, rapid and stable development, it needs to overcome a number of key constraints. Measures to remove the key constraints to achieve the long-term objectives include:

- Overcoming shortage of skilled manpower by increasing investment in education and skills training in technical and vocational subjects. Eritrea should develop the skills of its manpower with specializations in finance and management, law, applied science and medicine, and information technology— key for competitiveness and rapid economic growth;
- Improving essential infrastructure, especially increased access to power and water supply. Eritrea needs to expand its transportation and communications services in major cities and all other parts of the country. Good quality infrastructure in particular power and water supply is a prerequisite for attracting private investment and increased competitiveness;
- Adopting measures to mobilize adequate funds from domestic and external sources to finance investments. Severe foreign exchange gaps are serious constraints to Eritrea's development endeavors. By taking concrete steps, domestic savings particularly that of the diaspora and export

earnings will be enhanced to provide the foreign exchange necessary to import machinery, equipment and essential production inputs critical for achieving rapid economic recovery and growth. This will be achieved by adopting a well-articulated strategy of resource mobilization from internal and external financial resources and a more aggressive export development program (para. 3.25-3.29); and

- Accelerating the Peace Process. Uncertainties related to the demarcation of the border between Eritrea and Ethiopia and the peace process as a whole are detriments to investment, trade and growth. On April 13, 2002, the Eritrea-Ethiopia Boundary Commission (EEBC) published its binding and final decision on the demarcation of the border. While Eritrea has accepted the decision of the Commission in its entirety, Ethiopia continues to reject the decision and frustrate the process. This uncertainty is not helpful to economic growth and to regional peace and cooperation. Eritrea will continue to play a positive and constructive role toward the implementation of the final and binding decision by the Commission.

IV. INTERIM POVERTY REDUCTION STRATEGY

4.1 Keeping in view the factors responsible for slowing growth and increasing the incidence of poverty in Eritrea, the Government has formulated a comprehensive economic revival program aimed at reinvigorating economic growth and in the same vein a multi-pronged poverty reduction strategy aimed at addressing the underlying causes of poverty in Eritrea, which is outlined in this chapter.

4.2 Eritrea's Interim Poverty Reduction Strategy (I-PRSP) is anchored on the following four pillars:

- Pillar I: Rein vigorating Economic Growth
- Pillar II: Creating Income Earning Opportunities for the Poor
- Pillar III: Enhancing Access to and Utilization of Essential services for Human Development
- Pillar IV: Promoting Political, Economic and Social Participation of the population by putting in place the enabling environment

Pillar I. Rein vigorating Economic Growth

A. Adopting a Sound Macroeconomic Framework

4.3 Aimed at both stabilizing the economy and stimulating growth, the Government has developed a macroeconomic framework and a number of measures are being taken (Para. 3.25-3.4). The main components are reducing

the overall budget and current account deficits, lowering inflation, restoring growth and increasing the free reserves. Details on the macroeconomic framework and projected growth targets are in Chapter III.

B. Promoting Investment in Economic Sectors

4.4 Achieving rapid, broad-based and sustainable growth and poverty reduction requires not just macroeconomic stability, but also enhanced investment in sectors where Eritrea has a comparative advantage such as in agriculture, fisheries, manufacturing and tourism.

Agriculture

4.5 Recognizing the importance of agriculture to reducing poverty, enhancing national food security, and adding to exports earnings and support industrialization, the government conducted an agricultural sector review in 2001/02. Some of the critical challenges impeding the development of agriculture sector include limited water resources availability— emanating from deficiencies in storage capacity and poor on-farm water use efficiency, lack of application of modern farming techniques, poor marketing channels, and limited access to credit. Notwithstanding these constraints, there is significant potential in agriculture and livestock production. The critical elements of the policy include the following.¹²

- Increasing water availability. The most important challenge facing the agriculture sector in Eritrea is the shortage of water, which became especially acute in the face of the recent severe drought (Box 3.1). A substantial amount of water is lost every year in the system due to low on-farm water use efficiency. The strategy is to harness the seasonal water flows and direct them to where they are needed, through catchments rehabilitation, rainwater harvesting through construction of embankments, canals, lining of watercourses and introducing modern methods that enhance on-farm water use efficiency. Another is to store water to irrigate farm plots in seasons with low rainfall. The objective is to augment water storage capacity by constructing water reservoirs, small dams, diversion canals and wells and new irrigation schemes. The goal is to provide additional storage capacity of over 35 million cubic meters of water, bringing over eighty thousand hectares of land under cultivation and creating thousands of temporary jobs in the process.¹³

¹² Eritrea – Agriculture Sector Review, Ministry of Agriculture, 2002

¹³ Under the 2004 capital budget, nearly 100 million Nakfa is earmarked for water related infrastructure, mainly the rehabilitation and construction of water projects. Planning and implementation of these projects will be accorded high priority. Main segment of this program involves construction of micro-dams, much of it under Warsai Yekealo campaign.

- Furthermore, water saving measures such as rehabilitation of watercourses and land leveling and improved water application techniques at the farm level will be undertaken. Most of the watercourse schemes will be carried out with community participation and contribution in the cost of renovation and maintenance. Water tariffs for irrigation schemes will aim at recovering operation and maintenance costs and water charges will be adjusted upwards to reflect this cost recovery goals.
- Increasing farm productivity by introducing modern farming techniques and management methods and efficient on-farm water use by promoting wide spread use of modern farming practices – primarily farm inputs (increasing fertilizer and pesticide use) particularly on irrigated lands; wide spread use of improved pest control and reducing post harvest losses and developing and disseminating more drought-resistant, faster-maturing seed varieties. Soil conservation measures will be carried out to improve soil fertility and thereby crop production and productivity and to protect and restore the rural environment through terracing, construction of check dams, planting / afforestation through community participation and enclosure of natural vegetation.
- Promoting production of high-value crops. The Government will encourage farmers to produce high-value crops for export, commodities that can be used as raw materials for industry, and high-value cash crops that can substitute for imports. Horticultural products with export potential are oil seeds, cut flowers, cotton, sesame, fruits and vegetables, and tobacco. It is expected that existing cultivable area of 39,000 hectares will be cultivated with cotton and sesame, over the next five-years.
- Expanding land under cultivation.¹⁴. The goal is to bring under cultivation vast tracts of fertile land. This will enable farmers to intensify and diversify their agricultural production systems. The Government is formulating a policy to encourage corporate agriculture to bring vast tracts of uncultivated land under cultivation. This will not only encourage large investments in the agricultural sector, but also create job opportunities for rural residents and produce exportable surplus. The Government will encourage private investors, including those internally displaced people and Eritreans returning from Sudan or Ethiopia and those returning from the Diaspora to open new lands for cultivation. One such action is to provide concessions (e.g. land lease privileges to individuals and associations), to those that show

¹⁴ Eritrea has about 1.6 million hectares that is suitable for rainfed and irrigated cultivation, but are not currently farmed. This is particularly true in the Western Lowlands where the soil is fertile and stable, rainfall is reliable and application of modern cultivation and management methods possible

greater scope to quickly transform to commercial agriculture in eastern and western lowlands.

4.6 A number of other measures will be taken in support of modernizing the agricultural sector.

- Reorienting agricultural extension and research program to better respond more effectively to farmers' priority needs and demands. The research system should strive to develop crop varieties suitable for rain-fed and irrigated agriculture, identifying appropriate measures to reduce soil erosion, and mechanization that fits the terrain to overcome the shortages of labor and draft power. The Ministry of Agriculture will effectively transfer its commercial activities to the private sector, or corporatize public enterprises so that they are operated as commercial entities, while ensuring that essential inputs such as fertilizers, seeds, pesticides and veterinary medicines remain available during the period of transition. Increasing the MoA's extension and research capacity, including economic analysis of proposed new technologies.
- Increasing the flow of credit to the agricultural sector. The Agricultural and Development Bank (ADB) has been reorganized under a new management. The Bank will increase availability of adequate credit facility to support modernization of the agricultural sector and support small-scale enterprises.
- Constructing infrastructure and assisting in markets and marketing. Construction of rural infrastructure will be expanded, in particular road networks connecting potential agricultural areas like Gash Barka with major market centers. This will help farmers obtain better prices for their products and, thereby, earn enhanced incomes. Rural electricity for lighting and for operation of tube-wells for extracting ground water will also be provided.

4.7 Livestock Production. Eritrea has good potential for increasing earnings from production of livestock (goats, sheep, cattle, camels, pigs and poultry). The strategy focuses on modernizing and expanding livestock and dairy production by promoting modern production and management techniques, providing technical assistance pertaining to production, storage, transport, marketing and animal health and by providing incentives for private sector investment in modern production methods.

4.8 Priority measures include developing and rehabilitating breeding/hatching centers, and establishing bee-colony breeding and multiplication centers and systems for collection of milk. Technical advice and training will be provided to commercial producers, smallholder farmers, on modern production, marketing, and management techniques. Credit facilities

will be increasingly made available to small-scale commercial and semi-commercial poultry and livestock farms and distribution of chicks to needy farmers and female-headed households. Livestock and dairy producers and dairy farmers associations will be supported to increase their level of production and quality.

Fisheries

4.9 The fisheries of Eritrea are unique in the world today, in that they are not generally overcapitalized or over exploited.¹⁵ While many of the fishing areas in the world have been depleted and are yielding declining returns, Eritrean fisheries resources are still relatively healthy and in some cases under exploited. Therefore, Eritrea finds itself in a unique position of managing and exploiting a relatively young and healthy resource with the potential to offer great prospects for economic growth, meeting national food security objectives and earning foreign exchange for the country.

4.10 With a view to increase the contribution of the fisheries sector to Eritrea's economy, the following strategic objectives and priority measures will be pursued:

- Increase the profitability of the artisanal fisheries by strengthening the cooperatives of Artisanal fisheries through technical assistance for marketing, distribution, linking them to established high-value export markets, reducing import duties on fishing inputs to decrease their cost and assisting cooperatives to rebuild the stock of small pelagic fishery
- Boost export earnings by creating a suitable investment climate that would attract both national and foreign investors and enhance the profitability of industrial fisheries in the high-value export markets. The key measures are: adopting a sound investment policy for the sector that identifies major opportunities in fishing, processing, services and aquaculture; define specific incentive measures in fishing rights, tax regime, import duties on capital investment (e.g. Vessels, freezers) and inputs and approval process for granting incentives; stabilize the investment climate through government participation, investment guarantees, bilateral agreements to cover investment risk etc. and identify and select foreign investors with good reputation and profile; and
- Strengthen resource management and planning to serve as a catalyst to facilitate private investment and protect the environment. Key measures include: conduct of fisheries

¹⁵ Fisheries Sector Management and Development Action Plan , World Bank and FAO, (Draft Report, October 2003).

assessment and expand the current resource and fisheries monitoring program and adopt a sound vessel monitoring

4.11 The Government will continue to encourage private investment in modern fishing fleets and fish processing facilities, including through joint ventures with foreign investors. In 1998, a joint venture of the government with Italian and Dutch investors established a modern fish processing plant in Massawa at a cost of US\$ 1.2 million. The plant, Eri-Fish, is now exporting 150 tons of frozen fish every month to markets in Europe. New joint ventures with foreign investors are under negotiations. The completion of the International Airport in Massawa and the asphalted Asmara-Massawa road are expected to enhance trade and investment.

Manufacturing

4.12 Eritrea's small and medium enterprises (SMEs) sector holds great potential of generating employment, adapting technology, and creating an export base grounded in the country's true comparative advantage. The potential is particularly good in textiles and garments, leather goods, processed foods, fabricated metals, plastics, construction materials, and other resource-based goods. However, substantial investments are needed, and these are expected to come from domestic and foreign private sources. With a view to encourage foreign private investment, customs administration has been streamlined and a simplified corporate income tax regime established reducing the top rate on business income and treating tax loss carry forwards more favorably. A one-stop shop for business licensing is established and the process of acquiring land to investors will be simplified.

4.13 Furthermore, the Small and Medium Enterprise Development Unit (SMEDU) within the Ministry of Trade and Industry will be strengthened to develop programs that provide managerial and technical training and informational support to SMEs. The focus of the new organization is SME support, including easier documentation with financial institutions, free technical, managerial and marketing advice, information on sector situation, pre-feasibility reports, and access to trade information on various commodities. SMEDU will undertake a study to assess the bottlenecks impeding the growth of SME sector and devise a strategy and priority measures to enhance their efficiency and growth.

4.14 The Investment Center, a virtually ineffective organization is now being revitalized with a view to promote SMEs. For this purpose, the center is now under the new Ministry of National Development. In addition to SME development, the Government has also initiated export oriented sectoral initiatives particularly in agriculture, fisheries and manufacturing.

Tourism

4.15 Eritrea's pleasant climate and the warm waters of the Red Sea, with unspoiled beaches and offshore islands, and with marine life off the Eritrean coast augur well for the development of a dynamic tourism industry, however, substantial investment is required in hotel infrastructure, modern municipal facilities, transportation, telecommunications, and recreational facilities and general tourist services to achieve the desired long-term economic benefits in the sector.

4.16 The Government is taking important steps to develop the tourist industry: renovated the Asmara-Massawa road, asphaltting of Massawa-Assab road, constructing a new international airport in Massawa, and asphaltting of the "Felfel" road is being finalized. The government is encouraging private investors to open new hotels and restaurants and other hospitality facilities, and is privatizing or offering for private management all the hotels and related facilities under its control. Private investors in Massawa and the Dahlak Islands are constructing new hotels. Cultural tourism will be promoted in the rural areas of Gash-Barka region and "Felfel" in North-Eastern Mountains. The construction of Gash Setit Wildlife Park and camping sites and roadside lodges is a major initiative for jungle safari and tourist cultural centers will be developed along with other service facilities. Measures will be taken to protect Eritrea's natural environment and ensure that tourist activities do not negatively affect the environment.

C. Developing Critical Infrastructure

4.17 Communications System. Eritrea has an underdeveloped telecommunications services. While cities are connected with one another and to the rest of the world, towns and rural villages still lack services. In March 2004, the mobile telephone company has become operational and demand for mobile telephone service is expected to grow rapidly and reach 200,000 within five years. The country currently has four Internet service providers, all in Asmara, serving about 1,500 subscribers. The government is actively promoting Internet use by upgrading the system and telephone bandwidth. Since the telecommunication sector acts as a catalyst for growth of the Internet and other IT applications, the government is committed to the development and expansion of the telecommunication infrastructure in the country. To modernize and expand telecommunications services, the government plans to privatize the telecommunications network and attract foreign investment to upgrade it. New training programs by the public and private sectors are being launched to produce a pool of IT professionals. In addition the private sector is training IT professionals and data entry operators, which has a growing demand in the private sector.

4.18 Power. With the completion of the Hirgigo project, Eritrea's power generating capacity has now more than doubled. This is adequate to meet the demands for power in the medium-term. A Power Distribution Project is under preparation and will start implementation in 2005 with financing from the World

Bank and other development partners. The primary objective is to extend transmission and distribution lines beyond the major cities, towns and the rural communities

4.19 Roads. Although significant progress has been made since independence connecting the major cities and towns of Eritrea by road, the road network remains poor and inadequate. The road connecting Massawa to Asmara, the nation's busiest road, has been completely rehabilitated. The north-south coastal highway joining Mahmimet, Massawa, and Assab is under construction.

4.20 The Government has prepared a medium-term road development program with priority investments in trunk, feeder and rural roads. Priority is given to the maintenance and rehabilitation of existing road networks, to constructing rural and feeder roads, and improving links connecting the economically important sections with major markets in the country. The expansion in road network is prepared with sufficient consideration for the operating and maintenance cost implications in the long-term. The program also calls for increased involvement of the private sector in constructing and maintaining roads and includes proposals for enhancing road safety. The program is being supported with financing from the World Bank, the European Union and other development partners. The government is also studying options for further upgrading and expanding critical transportation services.

4.21 Railways. The old railway system has been rehabilitated starting with Asmara and Massawa segment and there are plans to purchase new locomotives, and accessories essential to run the railway. This is expected to be a critical transport link that would reduce the traffic congestion on the Asmara-Massawa road.

4.22 Air Transport. Recognizing that air transport acts as a catalyst for economic activity and growth, in April 2003, the new Eritrea Airlines became operational with highly trained and experienced Eritrean management staff, captains, flight crew and technicians, most of whom were senior staff with Ethiopian airlines until their expulsion by the Ethiopian government following the border conflict. These aviation professionals returned to Eritrea from the Diaspora where they have been working with various reputable airlines in the United States and Europe. Eritrean Airlines flies to Amsterdam, Rome, Milan and Frankfurt as well as to Dubai, Jeddah and Nairobi. There are plans to procure additional aircraft and extend the flying route to western and southern Africa and increase the frequency to Europe.

4.23 Ports. The port of Massawa is undergoing a major rehabilitation through a US\$60 million project financed by the government, the World Bank and Italy. This project consists of extending the berths, dredging, and land reclamation, construction of heavy-duty pavements for new container terminals, improvements of drainage, sewerage, and electrical works, and the building of workshops, warehouses, and equipment sheds. The rehabilitation of the port of

Assab is currently on hold. To enhance the efficiency and competitiveness of the ports, they are being operated as separate profit centers. Actions are also being taken to strengthen management capacities in both ports.

PILLAR II: CREATING INCOME GENERATING OPPORTUNITIES FOR THE POOR

4.24 While sound macroeconomic policies are essential prerequisites for ensuring poverty reduction, these policies may not automatically translate into a significant improvement in the living conditions of the poor. Therefore, to enhance income-generating opportunities for the poor, the second pillar of Eritrea's poverty reduction strategy is empowering the people and creating greater opportunities for increasing incomes of the poor. The strategy to be followed include:

A. Enhancing the Productive Capacity of Traditional Farmers and Fishermen

4.25 For the vast majority of the poor who live in rural areas, subsistence agriculture and related employment are the main sources of food and household income. One key element of the strategy is to enhance farm income and employment opportunities of poor communities by:

- Increasing Access to Farmland by poor farmers: In view of the positive impact that access to cultivable land has on food production and incomes of poor households, additional plots of available land will be distributed to poor farmers, supported with the provision of technical packages for grains and other crops, and effective application of fertilizer and other inputs. Priority will be given to women so they can equally benefit from such measures.
- Reorienting the extension and research system towards addressing priority problems and concerns of subsistence farmers. This covers effective extension packages in land preparation, cost-effective techniques in water harvesting, catchment rehabilitation, farm mechanization, and on-farm irrigation water use. Tractor ploughing services would be made available on a cost plus basis to farmers through appropriate credit mechanisms including from private sources. Availability of inexpensive technologies and inputs (such as drought tolerant, relatively high yielding crop varieties) and short cycle livestock (such as poultry, sheep & goats) are critical measures.
- Supporting building small dams to harness the seasonal water flows and supporting rehabilitation of degraded catchments by providing materials and equipment necessary for rehabilitation works and for runoff reduction. Priority measures on the catchments will include contour barriers, absorption ditches, terraces, micro-dams, check dams,

and planting trees and other vegetative ground cover. It also includes regulating grazing and conserving forage for use in the dry months. Communities that are organized for taking ownership of the individual programs will undertake catchment treatments. The first priority would be to treat over 7,000 hectares of degraded land.

- Developing and implementing integrated agro-livestock-rangeland support systems that address their input needs (seeds, veterinary medicine, animal feed and pasture, credit needs of the farmers), assure them reasonable returns by providing market information and marketing infrastructure and help mitigate their crop failure or livestock mortality risks (insurance). The objective is to enhance livestock production and the marketing system, particularly for pastoral communities¹⁶ in the main livestock producing areas in Gash Barka and Debub. This will be achieved by raising productivity, improving quality and expanding markets. The Government, will support the drilling of boreholes by providing credit for the purchase of necessary pumps, motors, overhead tanks, and pipe connections. The local communities will be organized into user associations and provided with training on how to operate the water points. Special attention will be paid to ensuring greater participation of women, especially female heads of households.
- Encouraging rehabilitation of small-scale irrigation systems by developing simple, low-cost gravity feed and pumped systems for community ownership and operation. The objective is to enable a year round agricultural activity and also diversifying into higher value crops. The proposed system is simple and labour intensive, and would provide employment for several thousand rural dwellers. High priority will be given to the development of smallholder irrigation schemes that have high levels of community participation in planning and cost sharing of the construction (mainly in labour) and full operation and maintenance (O&M) expenses. To encourage efficient utilization of water in agriculture for new water sector projects, water pricing will be put in place. Water prices for irrigation schemes will aim at recovering operation and maintenance costs, and for on-going irrigation schemes, water charges will be adjusted upwards to reflect this cost recovery goals.

4.26 Expanding Artisanal Fisheries. The Government will continue to support community based artisanal fisheries to increase the income of coastal villagers and enhance their household food security. To increase the profitability of the artisanal fisheries by strengthening the cooperatives of Artisanal Fisheries, establishing an area based co-management system between the Ministry of Fisheries and the co-operatives, assisting cooperatives to establish fully protected

¹⁶ Eritrea has a good potential for increasing earnings from livestock (goats, sheep, cattle, camels, pigs and poultry). This will be achieved by improving quality, raising productivity and expanding markets.

marine reserves in respective zones, increasing license fees for foreign fishers, issued by zone or group of zones, in conjunction with increased surveillance and enforcement, assisting cooperatives to rebuild the small pelagic fishery. Towards this end improving fisheries infrastructure (e.g. cold water facility, water desalination service, electric supply, flake ice machine, etc), and providing training, and strengthening fisheries' cooperatives in storage, processing and marketing is being undertaken. The Sahel Fisheries Development Project and the Barasole Community Fishing projects are supporting a total of 2,000 households in 25 fishing villages. Based on the experience and success of this model, similar community based artisanal fisheries will be established in other coastal villages.

B. Enhancing Opportunities in Micro and Small Enterprises

4.27 Promoting development of viable micro and small enterprises. Micro and Small-Scale Enterprises possess significant opportunities for job creation and enhancing income earning opportunities of the poor. To encourage the development of micro-enterprises such as poultry, bee keeping, food processing and small packaging, a model industrial estate that provides technical services and financial assistance to help start or expand businesses is being established in the outskirts of Asmara. Based on the experience and success of the model, similar estates will be established in the other administrative regions. Furthermore, the micro-industries centre in Medeber, in the outskirts of Asmara is being converted into a model industrial estate by rehabilitating the infrastructure, providing management and technical support service, training and counselling services. The objectives of such a pilot project are to improve product quality and design of local micro-industrial products and develop markets, both domestic and international, and to promote handicrafts, and micro-industrial estates.

4.28 Handicrafts and cottage industries also possess great potential for providing employment and income for the rural poor. There are a number of artisans making ornaments, jewelry, metal, clay, wood, and bead-based products, handloom weaving, etc. To enhance the contribution of women, a number of programs are being implemented that include providing training and support services to women entrepreneurs, and facilitate access to credit systems. The handloom sub-sector has been the priority sector for training and capacity building. The target beneficiaries are demobilized soldiers, women from under privileged sections of the society as well as displaced women from areas affected by the border war.

4.29 Improving access to micro credit is one of the key instruments to empowering and improving the income generating opportunities of poor or small enterprises. However, the poor are unable to get credit from the formal financial institution because they lack collateral and have a weak asset base.

4.30 With the aim of providing access to small enterprises, the Government is supporting two tiered micro credit program under the Eritrean Emergency

Reconstruction Program (ERP). The first tier provides small credit to individuals/groups, with particular attention to women headed households living in the poor rural and urban areas. Such loans are given to those applicants that meet two conditions: evidence that the borrower has a proven savings record of at least three months, and the applicant is a member of a solidarity group. Each group member is responsible for the repayment of loans defaulted by any of the other group members and none of the members will be given access to new credit until all loans have been repaid. The second system provides loans to small enterprises up to a maximum amount of Nakfa 43,000 based on the determination that the project proposal is viable and interview results and the profile of the applicant including satisfactory credit profile. This program operates in all six zobas.

4.31 The Government in collaboration with the UNDP has also initiated a 'Micro credit' component under the Food Security Capacity Building Project. The project aims at increasing the physical assets and incomes of the poor, mainly women heads of households in three targeted Zobas. The Savings and Credit program started first in the Northern and Southern Red Sea zobas and the second in the Anseba region is run by ACCORD – a local NGO. The three Zobas are beneficiaries because of their high incidence of poverty in these regions. The project is helping increase the income and employment opportunities of the poor in the poorest regions of the country.

D. Expanding Public Works Program

4.32 Public works schemes, such as Cash For Work will be expanded as essential instruments for employment and income generation for the poor, while at the same time improve the economic and social conditions of people living in the poorest and drought affected areas of the country. The program supports road rehabilitation and maintenance, soil conservation, forestry and water supply and sanitation schemes. They also contribute to improve people's access to markets and services and help in environmental protection and natural resource conservation.

4.33 The Government would expand the Eritrea Community Development Fund (ECDF), a demand-driven program ¹⁷ that finances economic and social infrastructure sub-projects: health (e.g. health stations, health centers), basic education (e.g. primary schools), rural water supply (e.g. boreholes and wells), soil and water conservation and afforestation, and rural feeder roads. To strengthen ownership and foster community participation, communities are required to contribute at least 10 percent of the project cost (in kind, cash or labor). Since female-headed households constitute a significant portion of the poor, the targeted programs focus on providing essential services namely water

¹⁷ The ECDF does not directly implement projects. Rather it supports the efforts of local communities by providing technical guidance and expertise in project management and implementation

supply, health care and nutrition services that rank high on the priority list of women.

PILLAR III. IMPROVING HUMAN RESOURCE DEVELOPMENT

4.34 Developing Eritrea's human resources capacity is one of the key strategies for attaining the goals and objectives of economic growth and poverty reduction. Virtually all policy related Government documents emphasize PEOPLE as the most valuable central resource that Eritrea has and on which the country will depend for its reconstruction and development efforts. The recently developed framework for human resources development 'Our People are our future' epitomizes this conviction. Progress in the education, health, and human welfare sectors are acknowledged as the key elements for improving human development.

A. Education

4.35 Since independence, the GoE has made major progress in adult education and expanding access to elementary and secondary education. For example, both the number of classrooms and the number children enrolled have almost doubled, several schools have been built in remote areas and educational opportunities and access to quality education has expanded. Despite these improvements, access to education remains inadequate. Significant regional and gender disparities exist. The quality of education is unsatisfactory as manifested in low learning outcomes, and high repetition and drop out rates, specially for girls and disadvantaged groups.

4.36 The Government has been working over the past three years on its overall strategy for the education sector and has produced several documents outlining its vision and national policy for the sector.¹⁸ Following from the policy, the Government has developed a National Sector Framework and Education Sector Development Program (ESDP) that translates the Government's vision of creating " a well educated and learning society" into action. The framework takes into account the very low enrollment rates, the resulting low probability of attaining the education for all and the MDG targets, and low achievement scores precipitated by the poor teaching and learning environment.

4.37 The education program will support:

- Increasing equitable enrollment in basic education through the construction of low cost but durable classrooms and ancillary facilities and targeted interventions aimed at girls and other disadvantaged children.

¹⁸ Eritrea – Education and Training Sector Note (February, 2003); National Education Policy (February, 2003), National Education Sector Framework (April 2003); Education Sector Development Program (December 2003)

- Improving the quality of basic and secondary education by expanding teacher training and professional support, replacement of expatriate teachers by Eritreans at secondary level; development of curriculum and pedagogical reforms.
- Developing technical skills and technology training by expanding existing technical schools and establishing new ones with due attention to cost-effectiveness, and the technical skills and training geared to meet labor market demand. Training will be imparted in trades selected in consultation with the local industry to create strong employment linkages.
- Strengthening sector capacity to deliver better quality education services by developing institutional capacity of the Ministry and Provincial Administrations in policy planning, management and monitoring and evaluation (M&E) to implement a rapid transformation of the education sector.

4.38 Recognizing the immense contributions of the private sector, the ESDP promotes partnerships between the private and public sectors to reach the goals of access and quality at all levels of education. It also supports an outreach program to facilitate Eritreans in Diaspora to teach in Eritrea (such as on leave of absence or other mutually agreed arrangements including summer vacation). Resource centers will be set up at Zoba and sub-zoba levels for providing decentralized information and capacity building opportunities to teachers, school directors and communities. These centers will have video-textbooks and libraries, which will be easily accessible to students.

4.39 Eritrea is committed to achieving the MDGs and the Education for all (EFA) goals. Activities under the ESDP are designed to contribute to the overall achievement of these goals. By successfully implementing the program, the Government would increase primary school enrollment and completion, enable more poor children to attend elementary and secondary schools, increase literacy rate and lower drop out rates of girls, and increase access to disadvantaged groups. By the end of the program period in 2008, the program aims to achieve an increase in Gross Enrollment Ratio (GER) in Primary Schools from 61% to 72%; Middle School from 44% to 50%; High School from 24% to 30%. Furthermore, it aims to reach GER level of 30 % in tertiary education including technical and vocational training; reduce adult illiteracy from 70% to 35% -all hallmarks consistent with the overall MDG targets.

B. Health

4.40 Eritrea has made great strides in improving the health status of its people. The Demographic and Health Survey (DHS, Para 2.2) report indicates an overall decline in early childhood mortality rates (infant, and under five

mortality).¹⁹ Government expenditures on public health (in constant prices) rose from Nakfa 108.2 million in 1997 to over Nakfa 113.5 million in 2001, or 3.3 percent of GDP in 2001). Despite these positive developments, access to primary health-care services remains inadequate and the quality of service delivery is poor.

4.41 The Government is committed to improving the health care system and making progress towards meeting the MDGs for the health sector. Its underlying principles are that improvements in health outcomes are an important determinant of economic growth and poverty reduction as better human health leads to improved learning ability and increased productivity. Towards this end, the Government adopted the National Health Care Policy (NHCP) and a health sector strategy (2000) that focus on primary and secondary levels.

4.42 The Government's medium term program will focus on prevention and control, especially in the area of communicable and infectious diseases, reproductive health, child health, and nutrient deficiencies for children under five and mothers. The Government launched the Primary Health Care Policy (PHCP) whose objectives are to minimize and eventually eliminate easily controlled diseases. Operated on the principles of community participation and a decentralized management system, the PHC policy targets four diseases that pose the most serious public health problems. These are HIV/AIDS, Malaria, Sexually Transmitted Diseases (STDs) and Tuberculosis or as is commonly known as HAMSET. The HAMSET project, jointly funded by the Government and the World Bank, is targeted specifically to address the threat posed by these four diseases. This project is on track and based on progress to-date, it is likely to meet its objectives.

4.43 An integrated Early Childhood Development Project (ECDP) is also under implementation. The main objectives are to develop early childhood education and care, improve child and maternal nutrition, strengthen child and maternal health services, improve nutrition education /public awareness and provision of vitamin A, iron and iodine, and support to children in need of special protection. The project is making satisfactory progress and upon completion is likely to meet its objectives. Moreover, institutional deficiencies in the health sector will be improved by strengthening human and financial capacity in the Zoba and sub-zobas health offices with a view to enhance their ability to effectively cater to the needs of the local population. Special attention will also be paid to developing healthcare services to the nomadic population who on average utilize less healthcare services than settled.

4.44 By 2005, the national health program aims to achieve immunization of 90 percent of children against antigens, eliminate iodine and vitamin A deficiencies and reduce iron deficiency by 33 percent. Furthermore, by 2006 the

¹⁹ Demographic and Health Survey, NSEO, 2002

target is to achieve infant mortality rate reduced to 40 per 1000 live-births (LB), under five mortality rate reduced to 85 per 1000 LB, deliveries attended by health workers increased from 32 percent to 45 percent, and reduce maternal mortality ratio from 230 to 150 by 2010. These goals are consistent with the overall MDGs.

4.45 Water Supply and Sanitation. Poor health outcomes are often associated with lack of access to water supply and sanitation. At present only 50 per cent of the country's population has access to safe drinking water (70 per cent in urban areas while 30 per cent in rural areas). Similarly, proper sanitation facilities are available to only 9 per cent of the total population.

4.46 The Government is committed to increasing access to water supply and sanitation services. This will be achieved by assisting rural communities in rehabilitating community water supply schemes and constructing new ones in collaboration with the private sector, NGOs and other development partners. The technical, planning and monitoring capabilities of the Zobas as well as the operation and maintenance capabilities of the communities will be strengthened. Water tariff will recover the full operation and maintenance costs and the community will cover at least 33 percent of the investment cost, either in kind or cash contribution.

4.47 To meet the city of Asmara's water needs, a reservoir has been completed at Tokker, about 25 kilometers northwest of Asmara. Construction is underway for supply of water and sewerage in Keren, Mendefera, Massawa, six towns in Gash Barka, and other small towns.

C. Protecting the Vulnerable

4.48 Meeting the basic needs of those who cannot provide for themselves is one of the main objectives of Eritrea's poverty reduction strategy. The goal is to improve social outcomes for all citizens, with particular emphasis on the vulnerable groups including women and children. This objective is to be achieved through targeted interventions and programs.

4.49 Women. To further advance the status of women in key economic, political and social life of the nation, ²⁰ the following steps will be taken:

Designate focal points in key sector ministries and public agencies to promote gender mainstreaming in national and sector policies and programs.

- Adopt a National Plan of Action (NPA) for women,¹⁸ with key policy reforms and programs for implementation in the immediate and medium-term; the prime focus of the program is education and skills

²⁰ The Eritrean constitution proclaims equality under the law. A National Union of Eritrean Women (NUEW) was established in 1992, an offspring of the National Association of Eritrean women which was part of the Eritrean Peoples Liberation Front (EPLF). Women played a crucial role in the war of independence – side by side with their male compatriots.

training, water supply, improving family health and nutrition and family planning in rural and urban areas²¹

- Enhance their economic empowerment by increasing access to land (farm and urban), improving access to water supply, micro-credit facilities to enable them to start self-help activities in agriculture and micro enterprises and enhancing their skills development through appropriate non-traditional job enhancing technical training

4.50 Disabled. The objective is to empower vulnerable and disadvantaged persons, including disabled war veterans, and the very poor. The Ministry of Labor and Human Welfare (MoLHW) is taking a number of steps to enhance their economic empowerment and providing skills training and job opportunities for those who are capable of engaging in employment and income earning opportunities. Several programs are under implementations that aim at the physical, social and psychological rehabilitation of disabled persons, including the community based rehabilitation of disabled persons in six Zobas. It also involves helping them to organize their own associations and do advocacy work for equal opportunity. Other programs provide essential food assistance, shelter, medical care, and other basic goods and services to the disabled war veterans. The program also supports rehabilitation of special education facilities for the blind and deaf, and skill-training facilities for all disabled aimed at job creation and transport services that ease their movement and mobility. MoLHW is running a handicraft school with the aim of transferring skill development to women.

4.51 Children. The Government in cooperation with development partners is engaged in several programs to assist disadvantaged children. The Orphan Reunification and Group Homes Projects aim is to protect the psychosocial and psychophysical interests of orphan children, by providing income-generating assistance, and stabilizing the socio economic situation of the host families; and to provide orphans a family like atmosphere and insure their integration in the community. The Support for AIDS Orphans Project provides financial support, education and skill training for the affected orphans, social, economic and psychological support for the HIV/AIDS orphans, training and building capacities among the caregivers of HIV/AIDS orphans, and building awareness among stakeholders including host families of HIV/AIDS orphans.

4.52 The MoLHW is implementing Street Children Rehabilitation Project that aims to prevent children from drifting to the street by rehabilitating street children, creating access to basic schools, providing income generating activities, providing vocational training and job placement opportunity, reunifying street children with their families, relatives or foster parents. A new project to provide care for the elderly is under preparation with the objective to

²¹ The National Gender Action Plan for Period August 2003 -December 2008, July 2003 NUEW.

provide financial support for the disabled elderly, and encourage the traditional safety net and increasing its effectiveness and treatment of the elderly.

4.53 The Government is currently developing a pension scheme. A task force recently finalized its draft recommendations. The draft pension report contains the draft laws and regulations for its establishment and operations including contributions. The Government committee is reviewing the proposed scheme. The pension scheme is expected to be operational in early 2004.

D. Affordable Housing and Shelter

4.54 Lack of adequate and affordable housing is one of the key indicators of poverty. Specific measures that would be taken to address this problem include: accelerating the planned construction of low income housing; exploring options to use domestically available construction materials in a cost effective manner; reviewing the institutional framework and clarify the mandates of the government agencies; addressing as a matter of urgency the inefficiency in urban land and housing administration including removing cumbersome and time consuming approval process; exploring and adopting new and innovative approaches in affordable housing finance, and encouraging the private sector to engage in the construction of low-cost housing.

E. Environment

4.55 At independence, Eritrea found itself with serious environmental problems. These included land and pasture degradation, deforestation, low quality of water for drinking and increasing deterioration of the urban environment. The Government established a Ministry of Land, Water and Environment, potentially providing for a more integrated approach to Eritrea's environmental problems. A comprehensive national environmental management plan has been adopted and is being implemented. National environmental assessment procedures and guidelines are in place. There exists a national biodiversity strategy and there is a program to protect marine biodiversity, supported by Global Environmental Facility (GEF).

4.56 The main objective of the National Environmental Management Plan (NEMP) is to enhance Eritrean environment that can sustain a healthier population, free from deprivation and free to attain the highest possible standard of living. The key measures include forest/ woodland closures, improved management of solid waste and sewage in Asmara and Massawa; promotion of renewable energy sources in remote rural areas; protection of Biological diversity; development of Coastal and Marine Protected area systems for Eritrea;

Pillar IV. Putting in place the Enabling Environment and Strengthening the Institutional Capacity

4.57 Strengthening the existing institutional capacity to plan, monitor and implement macroeconomic and poverty reduction programs is one of the cornerstones of Eritrea's economic growth and poverty reduction strategy. In fact, sagging growth and rising poverty are in part a reflection of poor enabling environment and weak institutional capacity to deliver services efficiently to the public as well as enforce the regulatory framework. Effective and sustainable poverty reduction is only possible when the enabling environment is in place and the legal and regulatory framework for sound governance is implemented.

4.58 Eritrea has put in place pertinent legal and regulatory frameworks. However, the institutional capacity and enforcing mechanisms are weak. The Government is committed to take the following important measures: (a) strengthening institutional capacity that enhances fiscal and financial accountability, (b) strengthening the capacity and reforming the civil service, (c) devolving power to the Zobas and ensuring popular participation of the population in all affairs of the nation building, and (d) enhancing access to justice. The success of Eritrea's poverty reduction efforts will depend, among others, on the real and measurable progress made in each of these areas.

A. Strengthening Fiscal and Financial Accountability

4.59 One of the pre-conditions for achieving broad based, sustainable and pro-poor economic growth is good economic governance in fiscal and financial activities. Toward this end, the following measures will be taken:

- Strengthening the existing public expenditure and financial management system. This will include an improved public procurement procedure that enhances efficiency and accountability.
- Improving public accounting and auditing functions by separating audit from accounts, and adopting a more modern best-practice public accounting system
- Instituting a procedure for systematic appraisal and approval of large public investment projects. This process would objectively assess and determine whether a program, project, policy or development strategy is technically and economically viable and is consistent with priority objectives of the country in the sector.
- Continuing the zero tolerance policy on corruption by enhancing institutional capacity to administer and enforce the rules and ensure accountability of public officials. The National Accountability Commission (NAC) was established in 1997 with powers to investigate and prosecute.

B. Strengthening and reforming the Civil Service

4.60 The PRSP process will require a civil service with enhanced professionalism and service orientation in ministries and public agencies. For this purpose the government has adopted a four-pronged strategy: aimed at strengthening the civil service, training of government officials, government right sizing, and improving remuneration of government officials.

4.61 A Task Force established to assess the training needs of the civil service has completed its report and its recommendations. A training program is being developed to improve the skills of civil service personnel, education and training infrastructure and financing requirements. The training program is expected to start implementation in mid-June 2004.

4.62 A Government Committee on Pension Reforms has finalized its recommendations on the new pension program. It is expected to be approved by the cabinet and start operating in March 2004. The new pension scheme called contributory fund scheme is being introduced for those currently in the government service and new entrants. In addition, the civil service reform committee's recommendation for salary reforms and to increase the pay of public service personnel is being reviewed. These together with other reforms will lay the foundations of a more rational and sustainable system of compensation for government servants.

4.63 Reform of Public Enterprises. The Government is committed not to be directly involved in commercial and business activities. To this end, it will re-invigorate the process of privatising remaining public enterprises and enhancing the efficiency of those that would not be immediately privatised. The public enterprise will be given full autonomy to operate and meet performance requirements in accordance with commercial practice.

4.64 A well-developed human resource base and sound institutions are one of the most crucial ingredients for achieving economic growth and poverty reduction goals. For this, effective and efficient public sector institutions are essential pre-requisites for the successful implementation of the strategy. The Government is committed to improve effectiveness in public sector management, and efficiency in service delivery and ensure effective public administration. This will be achieved through a short and medium term capacity building and training program that will be implemented to re-equip public services with the skills essential for efficient and effective service delivery. As a result, the general public and the private sector will gain better access to essential services; the poor will receive services at affordable prices and the full protection of the law as they strive to break out of poverty.

C. Devolution of Power and Enhancing Popular Participation

4.65 Strengthen capacity of regional Governments (Zabas). The Government is in the process of strengthening overall capacity of the regional administration/local governments so that they increasingly take responsibility to

deliver services and implement projects using more community based approaches. Their finances will be enhanced through the implementation of revenue sharing programs and increase their revenue mobilization and financial management capacity.

4.66 The Government is determined to devolving powers and responsibilities, including those related to social services, from the central to provincial levels to elected district level authorities and local council. Elections for regional council membership (regional parliament) will be held in May 2004. This will meaningfully devolve the powers to democratically elected local governments. This devolution of power is expected to strengthen governance by increasing decentralization, and accountability of administrative operations and people's participation in their local affairs.

4.67 In 2004, the provincial administrations have for the first time prepared their budget requests (capital and recurrent). The next step is to institutionalize financial decentralization with the aim of making more financial and human resources available to the regional administration and functionaries. This will require strengthening the budgeting and auditing functions at the regional levels.

V. PREPARATION AND CONSULTATION PROCESS ²²

5.1 This chapter describes the processes used to develop this I-PRSP and the consultation process with various national and international stakeholders including sector ministries, government agencies, private sector, non-government organizations, development partners and community members.

A. Institutional Arrangement

5.2 A National Steering Committee (NSC) was formed to guide and oversee the overall process of I-PRSP preparation. The NSC, which comprises the Ministers of National Development (Chairperson), Agriculture, Education, Health, and Labor and Human Welfare guided the overall work leading to the preparation of the I-PRSP. The Ministry of National Development [the former International Cooperation, Macro Policy and Economic Coordination unit in the Office of the President] led and coordinated the overall process.

5.3 A Technical Committee (TC) was formed under the direct supervision of the NSC. The TC was entrusted with the responsibility to coordinate and guide the various activities involved in the preparation of the strategy. They met periodically to review progress and ensure greater integration of various tasks

²² The UNDP provided financing to carry out poverty assessment and the overall task leading to the preparation of this draft strategy, and consultations with national stakeholders and development partners. The UNFPA also provided financial support.

that form an important input into drafting the strategy and ensure better integration of policies and programs in the strategy. The TC comprised representatives of the five sector ministries in the NSC, and the Eritrean Relief and Refugee Commission (ERREC), National Statistics and Evaluation Office (NSEO), National Union of Eritrean Women (NUEW), National Confederation of Eritrea Workers (NCEW) and National Union of Eritrean Youth (NUEY).

5.4 The preparation of the I-PRSP in tandem with the Food Security strategy was a major challenge, both in terms of content and process. The main steps involved organizing and carrying out a national household survey (LSMS), and a complementary participatory poverty assessment (PPA) in which quantitative and qualitative data was collected. This was followed by an analysis of the data and a report on the nature, severity and underlying causes of poverty. Sector ministries, national NGOs and the Chamber of Commerce and Employers Association prepared a report which summarized their main achievements since independence, key challenges and the main elements of their sector policy and priority programs in the medium-term, designed to promote rapid economic growth and assist the poor in the form of employment generation and income-earning opportunities. These sectoral reports from the various agencies provided essential inputs for formulating the I-PRSP and a Food Security Strategy.

B. Consultations with Key Stakeholders

5.5 Consultations with all stakeholders, in particular the community groups is recognized as a critical component of the process of formulating the poverty reduction strategy. The GoE adopted a framework for participation that advances the following goals: (i) to ensure country ownership; (ii) to allow the various stakeholders to exchange views and expectations; (iii) to ensure that the strategy addresses the priority needs of the poor and reflect local realities; and (iv) to enhance the chances that key stakeholders, including development partners, buy-into the process and overall direction and content of the strategy.

5.6 This draft interim strategy has been prepared through a participatory process that provided opportunities for dialogue with key national stakeholders. The objective of this consultation process was to elicit views, share experiences, and understand expectations of the stakeholders while formulating the poverty reduction strategy. Principally, it served as a forum where stakeholders influence and share experience on the overall direction of the strategy and the priority measures based on international experience under similar settings.

5.7 The consultation process to develop the I-PRSP was completed in stages. It involved consultation with key partners to review three important products that were distributed to them in advance. The products consist of (i) a concept paper which outlined the overall framework, work program, timetable and resources needed; (ii) the approach and methodology to be used in conducting the field surveys (LSMS and PPA); (iii) poverty assessment covering the extent, severity and geographic distribution and perceptions of the poor; and (iv) the

main elements of the proposed strategy and the near and medium-term priorities and programs.

5.8 The process first involved consultation with key government entities, civil society, private sector and academia.²³ Consultation was also conducted with development partners at the various stages of the process with a view to draw lessons of international experience and best practice related to process and content of a poverty strategy. The development partners provided timely and constructive feedback, both early in the process and on the draft report. The revised I-PRSP takes into account the various comments received from stakeholders.

5.9 The GoE presented this strategy to all stakeholders during July - September 2003. Participants included government officials from sector ministries and local administration, development partners, civil society organizations, business and workers' associations. Similar consultations were also organized with local government and community representatives in the Zobas to solicit their views and to ensure broad ownership and support for both the process and content of the strategy. This draft I-PRSP has been revised to reflect the valuable feedback obtained from consultations with national stakeholder and development partners.

C. Key Messages that Emerged from Consultations with Community Members and representatives in the Regions

5.10 Consultations were also held with representatives from Zobas, private sector and NGOs operating in these areas and the target population to inform and discuss the overall focus of the strategy, priority measures and public programs. They provided a reality-check on the perceptions of the people and the implementation agencies including NGOs on the strategy and realities on the ground and feedback on whether public programs address the priority needs of the communities.

5.11 The consultations highlighted the fact that poverty reduction efforts need commitment at all levels of society and community groups should be associated in these efforts. The Government should continue this process of local consultations to build ownership and gain support of all stakeholders. For this purpose it was necessary that the community members expressed their priorities and actions. Similarly, they recommended that sound monitoring mechanisms be put in place to track and monitor these policies.

5.12 The following are the summary recommendations of the consultations with communities:

²³ The UNDP provided funding to carry out the field surveys covering the LSMS (quantitative) and Participatory poverty assessment, analytical work, and the preparation of the report and consultation process.

- The nation's number one preoccupation is peace and national security related to the recent border war with Ethiopia. The community representatives expressed that implementation of the decision of the Border commission should start without delay and this would allow the demobilization and reintegration of combatants to civilian life.
- Food assistance to mitigate the severe drought as a temporary measure. Perhaps the most valuable view expressed during these consultations was that they do not like to depend on government handouts on a regular basis. The participants contended that the government should focus its attention on creating opportunities for jobs that can give them a decent living with dignity and respect. These opportunities should relate to income earning possibilities outside agriculture, access to basic services in education and health and infrastructure, in particular rural roads and electricity
- The government should be actively engaged in developing economic and social infrastructure, particularly water supply, roads, schools, hospitals, training and skill development facilities; these have direct impact on poverty reduction and improving their living conditions.
- The government should focus its activities on a few critical areas, mainly employment generation and provision of water supply and rural roads (linking farms to markets). Employment generation through public works programs and other income earning opportunities are considered critical.
- The agricultural sector should be developed through an adequate extension system that includes timely availability of critical inputs and access to credit facilities
- Zoba level capacity building is necessary for effective implementation of government policies and programs.

5.13 The consultation held with key stakeholders in the six provinces encouraged broad public participation in poverty reduction efforts and evoked ownership at the level of provinces, national NGOs and community leaders. These consultations have not only built greater ownership among the Zoba governments but also elicited inputs from them in terms of developing a nationally consistent monitoring and evaluation mechanism for tracking expenditures, monitoring policies, and assessing impact on the (agreed) final set of I-PRSP outcome indicators. Most importantly, this round of dialogue has underscored the point that there are essential similarities and differences in the nature of poverty across different Zobas and that a single approach will not be adequate. Accordingly, allowance will have to be made for peculiarities and varying contexts presented by each Zoba.

VI. MONITORING AND EVALUATION MECHANISMS

6.1 Building the National Data Base. Eritrea inherited a poor statistical database and monitoring mechanism that includes lack of a statistical legal framework, and a weak institutional capacity for national and sectoral national database. The current monitoring and evaluation systems are inadequate with poor data collection and analysis and lack of clear arrangements for monitoring and evaluation. There is also a general lack of adequate use of results from monitoring and evaluation for policy formulation.

6.2 Poverty Reduction Strategy Monitoring System. Availability of reliable data in a timely manner is a key element of economic growth and poverty reduction strategy. With a view to strengthening the mechanisms for monitoring and evaluation (M&E) the proposed strategy and the effectiveness of policies and programs in reducing poverty, the Government is committed to developing a sound system that monitors performance and provides feedback. The following measures will be taken as a matter of priority:

- § Generating information and increasing capacity to analyze and disseminate it;
- § Monitoring progress in the implementation of the policies and programs as part of the poverty reduction programs with a view to identify the key constraints that impede progress and draw lessons of experience and
- § Helping to determine whether the key actions (policy, institutional and investments) being implemented are having the intended effect on poverty reduction

6.3 Monitoring Mechanisms. The success of Eritrea's poverty reduction strategy (PRS) will depend upon the institutionalization of implementation mechanisms that not only track poverty related expenditures but also monitor key intermediate success drivers (or catalysts) and outcomes.

6.4 In monitoring progress of the PRS indicators, the government will strengthen the technical and institutional capability of the various departments and agencies involved in information collection and analysis. In this entire process MOND will provide overall lead and act as a facilitator in terms of capacity building and support. It will ensure that proper institutional arrangements are put in place for overseeing implementation right from expenditure monitoring to outcome analysis and then feeding this information into overall policy formulation.

A. Tasks to be Performed

As a first step, a list of I-PRSP expenditures (inputs) will be developed with the participation of ministries and Zoba administrations. The timely availability of these resources will be crucial for achieving the desired growth and poverty reduction objectives. These expenditures are expected to be consistent with the overall macroeconomic framework and the levels/magnitudes will be maintained and tracked over the medium term. A summary of the budgetary resource requirements will be provided. The requirements will be classified into (1) Economic Services and others (irrigation, land reclamation, rural development, food assistance), (2) Social Sectors (education, health, population planning, social security, natural calamities & other disasters), and (3) Infrastructure (water supply & sanitation, roads, highways & bridges). The principal objective will include improving human development, increasing production and productivity in economic sectors, enhancing the employment and income earning opportunities of the poor, strengthening the enabling environment for private sector growth, supporting the poor and the most vulnerable individuals and groups, and building institutional capacity, for implementing policy reforms and investment programs to achieve poverty reduction goals. An effort is being made to devise sound procedures and institutional mechanisms for regular tracking of poverty related expenditures at the national and Zoba levels.

6.6 The expenditure tracking exercise will be linked with the achievement of selected poverty reduction targets, and sectoral indicators mainly in education, health, water supply and sanitation, nutrition, housing, food and other assistance programs in support of the vulnerable) as well as cross-cutting targets (gender, micro-credit, environment and capacity building). These indicators and targets will be rationalized, along with consistent measurement methodologies, benchmarks, and sources in consultation with zoba administrations, and concerned departments/agencies. All data producing entities and users will be involved in this process.

6.7 A preliminary poverty reduction-monitoring matrix (Annex 1) is being prepared and will be finalized based on feedback from concerned parties. The matrix contains three components: (a) expenditure tracking, (b) output mapping and (c) outcome monitoring. For instance in the case of education, the efficiency of expenditures incurred on teacher training will immediately be seen in terms of the intermediate/output indicator, proportion of trained teachers; while its relatively long term impact would be visible in terms of better enrolment and lower repetition rates. However, it must be mentioned that some key input indicators may not have easily identifiable corresponding monitorable output/intermediate and outcome indicators.

6.8 Evaluation Mechanism. To evaluate progress on the poverty reduction indicators, regional administration offices will identify focal points within their respective desks. These monitoring units will track progress, in close coordination with district administrations, on intermediate and outcome indicators and report periodic progress to the monitoring and evaluation unit at the Ministry of National Development (MoND).

6.9 The MoND will lead the effort to develop and institutionalize a sound poverty monitoring system in stages at the national and zoba levels. The NSEO under the Ministry will assemble information relating to inputs (expenditures), output/intermediate and outcome indicators from the zoba monitoring units and other concerned departments. This data will then be analyzed to assess the impact of poverty reduction policies and investment programs on the poor. It will also produce periodic progress reports on the final PRSP indicators. To ensure the success of this system, the capacity of the MoND staff will be strengthened in data analysis and reporting on PRSP indicators.

6.10 Instituting a sound mechanism for preparation and monitoring of PRS will require significant capacity both at the sector ministry and provincial administration levels. Four key areas where this need is particularly pressing are: (a) data collection and analysis covering key poverty indicators, (b) preparation of PRSP and conducting dialogue with stakeholders including civil society, (c) monitoring (data collection, impact assessment), and (d) special studies and surveys (in depth and continuous analysis of poverty profile in selected areas). These needs cut across all levels of government. The costs involved in creating these capacities will consist of temporary staff (with skills in office technology), procurement of office equipment, provision for technical assistance mainly to engage consultants to undertake special studies and workshops. A detailed estimate of these costs is being worked out.

B. EXPECTED RESULTS/OUTPUT INDICATORS

6.11 Two important landmarks will be achieved.

1. A sound institutional mechanism and a quality monitoring system developed. The new monitoring system:
 - Builds the various data sources and analytical tools for monitoring; the different tools for organization, storage and dissemination; and the institutional issues arising when setting up a monitoring system
 - Establishes a monitoring framework: defining clear goals, identifying targets and indicators, developing a system to track indicators (assessing data needs, collection and analysis, institutional structure)

- Carries out case studies on poverty monitoring experience in other countries
 - Applies analytical tools for monitoring: simulations for social indicators and poverty (SimSIP)
 - adopts key techniques and tools available for monitoring, with special focus in implementing a monitoring system within the PRSP process and implementation including the MDGs.
2. Capacity of various central ministries and provincial administration in Poverty Monitoring strengthened:
- Carried out a diagnosis and defined priority M&E capacity building measures, aimed at addressing the constraints in data collection, analysis, monitoring and reporting and the appropriate capacity building measures that would be required to strengthen the M&E capability in the implementation of the PRSP.
 - Identified areas that would have to be strengthened (e.g. Planning, audit and financial management, monitoring, procurement, etc) in terms of human resources development.
 - Prepared and conducted training to participants (Economists, statisticians or other sector professionals) on the various tools and techniques available for the monitoring of poverty and interventions, placing emphasis on PRSP targets and goals
 - The various sector ministries and Provincial administrative branches will be equipped with necessary theoretical and practical skills of M&E, planning, financial management, audit and accounts, procurement.

Timetable for Processing

Sector/Area	Process Indicator	Target
1. PRSP	-Draft IPRSP -Revised I-PRSP Completed -Consultation Conducted - I-PRSP completed - Full PRSP	-July 2003 -November 2003 -July- November 2003 -February 2004 June 2004
2. Food Security	-Draft FSS completed	-October 2003

	-Consultation -Final FSS	-July - October 2003 -February 2004
--	-----------------------------	--

From I-PRSP to Full PRSP

The Interim Poverty Reduction Strategy Paper (I-PRSP) contains the following four core elements:

- Poverty diagnosis
- A description of the country's participatory process
- Arrangements for monitoring & evaluation system, and
- The Macroeconomic Framework and key elements of the strategy and priority public actions.

Box 6:1 Full PRSP (from March to July 2004).

During the next few months, a Full PRSP will be prepared with the following information:

A. The Macro-economic framework

The full PRSP will strengthen the section on macroeconomic policies (monetary, fiscal and foreign exchange policies) and directly related structural reforms. Specifically, the full PRSP will assess to determine that:

- The macroeconomic framework promotes a level of inflation that does not undermine private sector growth, an external position that is sustainable in the medium to long-term, a growth rate that is consistent with poverty reduction objectives, and an overall fiscal stance that is compatible with the poverty reduction and growth objectives. (A table(s) presenting the country's macroeconomic framework)
- the growth projections are realistic and take into account likely sources of growth, including external assistance and likely increases in external trade and investment from Eritreans in Diaspora.
- The trade-off between the pursuit of short-term and long-term poverty reduction and other macroeconomic goals are realistic
- The macroeconomic policies and programs are robust including their ability to withstand exogenous shocks in the light of the risks of exogenous shocks (provide alternative scenarios for expenditure)

B. Priority public actions

- Summary of the priority public actions over a three year horizon
- A matrix of key policy actions and institutional reforms (including capacity building measures in public expenditure management, budget execution and fiscal and financial accountability) and target dates for their

implementation.

- Main risks that inhibit the successful implementation of the PRSP and indicate mitigation measures

C. Fiscal Choices (Public Expenditure Program)

- The allocation of expenditures is consistent with the strategic priorities, institutional capabilities and efficiency and realistic cost estimates
- The fiscal choices are consistent with the poverty reduction and growth objectives of the PRSP
- Details of financial resources that would be allocated for increasing production and productivity in economic sectors, improving human development, enhancing employment and income earning opportunities for the poor, protecting the very poor and the most vulnerable against shocks, and building institutional capacity for implementing reforms outlined in the I-PRSP. * (Table 1 below)
- Present a table(s) summarizing the overall public expenditure program and its allocation among key areas. ²⁴

D. Targets and Monitoring Indicators

- A more developed monitoring mechanism and arrangements for monitoring and evaluation to assess the effectiveness of the strategy and priority actions and associated public expenditures
- Expected outcomes (monetary and non-monetary) and establish specific indicators of progress and set annual targets. These indicators and targets should be consistent with the overall objective of poverty reduction and the institutional capacity to monitor results.
- Intermediate indicators and targets for the timely monitoring of performance. The indicators will include those related to international development goals.

²⁴ Data on the public expenditure program will include all activities financed by budgetary sources as well as other sources (bilateral and multilateral assistance, non-governmental organizations and community groups). It will also indicate increases in revenue from improvements in tax administration and efficiency and resources from external assistance and increased foreign investment including from Eritrean's in Diaspora.

Budgetary Expenditures (2004-06)
ACTUAL Budget Expenditures (2002 and 2003) and PROJECTIONS (recommended for 2004)
Capital and Current Expenditures

Economic Sector	2002 *		2003 *		2004		2005		2006	
	Nakfa Millions	As a % of GDP	Nakfa Millions	As a % of GDP	Nakfa Millions	As a % of GDP	Nakfa Millions	As a % of GDP	Nakfa Millions	As a % of GDP
A. Infrastructure										
1. Roads, Highways & Bridges										
2. Water Supply & Sanitation										
B. Social Services										
1. Education										
2. Health										
3. Population Planning										
4. Social security										
5. Natural Calamities & other Disasters										
C. Economic Services and Others										
1. Irrigation										
2. Land Reclamation										
3. Rural Development										
4. Food Assistance										
D. TOTAL (A+B+C)										

Source: Ministry of Finance (2002, 20 03) and Ministry of National Development (estimates and projections)

ERITREA
INTERIM POVERTY REDUCTION STRATEGY (I-PRSP)
POLICY MATRIX

PILLAR I: ENGENDERING GROWTH

A. Sound Macroeconomic Framework			
Area	Objectives	Strategies and Measures	Expected Output
I. Economic Growth & Stability	<p>Attain rapid and widely shared economic growth with macro-economic stability and steady and sustainable reduction in poverty.</p> <p><u>Transition</u>: meet the significant urgent humanitarian needs, redress the fiscal and monetary imbalances, reinvigorate the economy by releasing manpower; and restore the development momentum</p> <p><u>Medium-long term</u>: achieve macro-economic stability and growth</p>	<ul style="list-style-type: none"> - Promote competitive private sector development by effective public sector management and strong public-private partnership - Pursue sound fiscal, monetary, trade and investment policies that mobilize and allocate resources efficiently - Attract private sector investment and expand exports and develop a sound financial system. - Implement demobilization program in reduction in defense expenditure and inject a large pool of manpower into the economy 	<ul style="list-style-type: none"> - Macroeconomic imbalance redressed and the economy showed good growth rates - GDP grows by 6% (2004-05) and by 7-8 percent in 2006 - Fiscal deficit (including grants) falls to 20, 15, and 10 percent of GDP in 2004, 2005 and 2006 respectively - Inflation decreases to 15% in 2004, 10% in 2005 and 5% in 2006 - Official reserves reach 1.5 and 2 months of imports 2004 and 2005 respectively and 3 months in 2006
1. Fiscal Policy	<ul style="list-style-type: none"> - Establish a tax structure that substantially improves mobilization of revenues, promotes efficient use of resources, provides incentives to 	<ul style="list-style-type: none"> - Implement tax reform to further simplify and streamline tax system, broaden tax base and improve efficiency of tax administration - Increase the level of cost recovery on public utilities and increase revenue from the sale 	<ul style="list-style-type: none"> - Simplified and efficient tax system and administration put in place - Tax revenue increased moderately relative to GDP in 2004 – 2006 - Budget deficit declined from 29 percent of GDP in

	<p>investors and achieves greater equity</p> <ul style="list-style-type: none"> - Reduce the fiscal deficits to acceptable levels as percentage of GDP (to reach pre-border conflict levels) 	<p>of public properties</p> <ul style="list-style-type: none"> - Strengthen public sector financial management by adherence to budgetary discipline, sound planning and budgeting - Adopt austerity measures on capital and recurrent spending for 2003-06 	<p>2002 to about 15 percent in 2004 and xxxx in 2005 and 2006 respectively</p> <ul style="list-style-type: none"> - Demobilization program resulted in significant reduction in defense expenditures
2. Monetary and Exchange Rate Policies	<ul style="list-style-type: none"> - Achieve macroeconomic stability and external sustainability - Create the macro economic conditions that support growth and stability and the establishment of a dynamic financial system 	<ul style="list-style-type: none"> - Bank of Eritrea (BoE) strengthen its core central banking functions and restrain expanding the monetary base and restrict provision of credit to the Government - BoE maintains price stability while influencing credit and interest rate that promote growth - Adopt a more flexible exchange system that will lead the official exchange rate to adjust to the market rate 	<ul style="list-style-type: none"> - Inflation decreased from an estimated 18% in 2003 to 15% in 2004, 10% in 2005 and 5% in 2006 - The official exchange rate adjusts to the market rate and an auction mechanism for official reserves established - Official reserves increased from 1 month of imports equivalent in 2003 to 1.5 months in 2004, 2 months in 2005, and 3 months in 2006.
3. Trade and Investment Policy	<ul style="list-style-type: none"> - Maintain an open and liberal trade policy that promotes regional economic cooperation - Promote an outward looking, private sector led market economy - Widen the export base and reduce the current account gap 	<ul style="list-style-type: none"> - Eliminate or reduce all trade barriers, lower the number of import tariff rate including the maximum Level - Streamline customs administration procedures required for importers before they obtain clearance - Encourage foreign investment in all sectors without restrictions to the ownership or capital structure - Establish a Special Commission responsible to promote investment by Eritreans in Diaspora 	<ul style="list-style-type: none"> - Domestic and foreign investment increased including from Eritreans in Diaspora in key sectors of the economy - Investment by Eritreans in Diaspora increases and becomes source of revenue and balance of payment support - Current account improves with rapid expansion of exports and increase in foreign investment
4. External Finances and Debt management	<ul style="list-style-type: none"> - Curtail growth of domestic public debt and external borrowing to a level consistent with low inflation, and without crowding out the private sector in the credit market 	<ul style="list-style-type: none"> - Reduce domestic borrowing from Banks and financial institutions - Seek grant assistance to the fullest extent and external financing on favorable terms - Finance development projects, in the form of grants or hybrid of grants and loans on 	<ul style="list-style-type: none"> - Growth of domestic public debt and external borrowing curtailed - New external debt contracted only on IDA or better terms

	- Ensure that domestic and external debt burden is reduced to sustainable level as of GDP	concessionary terms from multilateral and bilateral sources	
B. Increasing Investments in Economic Sectors			
Area	Objectives	Strategies and Measures	Expected Outcome
1. Agriculture	<ul style="list-style-type: none"> - Enhance domestic food production - Supply raw materials for industrial and agribusiness purposes - Increase foreign exchange earnings 	<ul style="list-style-type: none"> - Develop and disseminate drought resistant, fast maturing seed varieties - Improve soil fertility by conservation measures - Promote production of high-value crops for export - And domestic consumption - Expanding land under cultivation - Increase water availability and water efficiency - Increase availability and flow of credit to agricultural Sector and expand micro-finance programs for Small investment activities at the local level 	<ul style="list-style-type: none"> - Increased land under cultivation by commercial farmers - Increased credit to the agriculture sector particularly to women - Strengthened research and extension services increased yields and total production of basic crops - Reduced post harvest losses and soil erosion - Rehabilitated water catchments and storage - Increased yields and total production of high-value crops - Increased cultivated area in Western Lowlands to 39,000 Hectares 2004-2006 - Increased water storage by 35 million cubic meters
2. Livestock	Modernize and expand livestock and dairy production	<ul style="list-style-type: none"> - Promote modern production and management, Techniques - Provide incentives for private sector investment in modern production methods - Develop and rehabilitate breeding/hatching centers for bee colony production - Establish a modern system of milk collection - Increase the availability of credit to small-scale, and commercial poultry and livestock farms 	<ul style="list-style-type: none"> - Increased livestock products - Increased sanitary storage and transport of livestock products - reduction in the incidence of animal diseases - increased availability of breeding/hatching centers - increased flow of credit to the livestock sector including women established dairy producers associations.

3. Fisheries	Exploit the large untapped potential to enhance national food security and foreign exchange earnings	<ul style="list-style-type: none"> - creating a suitable investment climate for the industrial fisheries - strengthening fisheries resource management and planning 	<ul style="list-style-type: none"> - foreign private investment increased in the sector, a dynamic and modern fisheries industry evolves with great potential for export - sector contribution to growth, foreign exchange earnings and national food security increased markedly
4. Manufacturing	<ul style="list-style-type: none"> - Increase the sector's contribution to economic growth, foreign exchange earnings and employment generation - Promote private investment 	<ul style="list-style-type: none"> - provide export promotion support - promote SMEs through skills training in managerial, technical and marketing and IT and access to trade information on manufacturing products - Revitalize the Investment Center to promote SME oriented towards exports especially in agriculture, fisheries, manufacturing and tourism sectors 	<ul style="list-style-type: none"> - Number of successful SME with export base increased - Sound base established for export, industrial base diversified and manufacturing output increased, exports and foreign exchange earnings increased - demand for training and advisory services of the IC increased
5. Tourism	Exploit the prospects for economic growth and foreign exchange earning.	<ul style="list-style-type: none"> - promote foreign and domestic private investment to develop and open new hotel infrastructure and other hospitality facilities - expand recreational facilities such as hiking lodges; restaurants and bird-view points - renovate architectural heritage and promote cultural tourism in the in rural areas - develop communication facilities 	<ul style="list-style-type: none"> - new hotels and hospitality facilities constructed - Masswa and Dahlak islands start developing as tourism attraction centers - physical infrastructure and tourism facilities laid down for expansion of the tourism industry - hotels and related facilities under government control privatized

C. Investment in Infrastructure

Area	Objectives	Strategies and Measure	Expected Outcome
1. Communications system	<ul style="list-style-type: none"> - Improve Eritrea's competitive position, economic growth and integration of all regions through an efficient and modern system - develop and expand the telecommunication 	<ul style="list-style-type: none"> - launch mobile telephone and expand rapidly - actively promote Internet use by upgrading the system and telephone bandwidth and expand internet service users in Asmara and throughout the country - modernize and expand telecommunications 	<ul style="list-style-type: none"> - training programs launched by the public and private sectors produce a pool of IT professionals and data entry operators. - telecommunication services serves as a catalyst for growth of the Internet and other IT applications - the number of subscribers to mobile phone and

	infrastructure in the country to enhance Import & Export trade facilities	services by privatizing it.	internet reached 200,000 and 10,000 in Asmara and other towns in five years
2. Power	Develop a reliable and adequate power generating capacity to meet the national demand up to 2015	implement a project starting in 2005 to extend power lines beyond the major cities and towns to the rural communities	adequate supply of power to meet the national demands in an effective and efficient manner extended
3. Roads	<ul style="list-style-type: none"> - Establish an efficient and adequate road network connecting cities to population centers and high potential areas - Enhance Eritrea's competitive position in trade and investment and facilitate growth 	<ul style="list-style-type: none"> - invest in economic infrastructure, including rehabilitation and expansion of highways and road networks - expand road network with sufficient consideration for the operating and maintenance cost implications in the long - term. - increased involvement of the private sector in constructing and maintaining roads and enhancing road safety. 	<ul style="list-style-type: none"> - the road connecting Massawa to Asmara expanded and asphalted - the north-south coastal highway joining Mahmimet Massawa, and Assab completed - major cities and towns of Eritrea connected by road, and the road network including feeder roads facilitating transport, trade and investment - the road network links the economically important sections of the country with major markets in the country
4. Railroad	<ul style="list-style-type: none"> - Develop a critical transport link to reduce the traffic congestion in major highways connecting with Asmara - develop a more cost effective means of transportation to facilitate trade especially for cargo 	<ul style="list-style-type: none"> - rehabilitate the old railway system starting with Asmara and Massawa route and purchase new locomotives, and accessories essential to run the railway. - Rehabilitate Asmara – Akordat segment and facilitate transportation of agricultural produce from Gash Barka to major market centers and the port of Massawa 	<ul style="list-style-type: none"> - traffic congestion reduced significantly and viable and cost effective services in - transport facilities especially for goods improved
5. Ports/Air links	<ul style="list-style-type: none"> - Enhance efficiency and competitiveness of the ports of Massawa and Assab - Develop air transport to facilitate trade and investment and serve as a catalyst for economic growth 	<ul style="list-style-type: none"> - Rehabilitate the port of Massawa - Operate Massawa and Assab ports as separate profit centers and strengthen management capacities in both ports. - Launch new Eritrea Airlines managed and operated by highly trained and experienced national staff 	<ul style="list-style-type: none"> - the port of Massawa completely rehabilitated - both Massawa and Assab ports operate as separate profit centers and - a new Eritrea Airlines launched and facilitates transport of people and goods.
6. Water supply	Increase access to reliable water supply and sanitation and improve the productive capacity and health	invest in both urban and rural water supply systems by installing new rural water supply and sanitation systems and rehabilitating	undertake a comprehensive assessment of water resources in 2004. This will become the basis of a national water resources policy and investment

	status of the population	<p>old ones.</p> <ul style="list-style-type: none"> - providing financial assistance to cover portion of the total cost - provide training and technical assistance so that communities are fully responsible for managing them and financing their operations and maintenance. - Raise water tariffs to cover capital, operating and maintenance costs of urban water delivery systems and to encourage users to conserve water 	<p>program.</p> <ul style="list-style-type: none"> - reservoir at Tokker, about 25 kilometers northwest of Asmara constructed - water supply and sewerage systems constructed in Keren, Mendefera, Massawa, six towns in Gash Barka, other small towns - water supply system installed in several rural communities in the country
Pillar II. Creating Income Generating Opportunities			
Area	Objectives	Strategies and Measures	Expected Outcome
1. Agriculture and Fisheries	<ul style="list-style-type: none"> - Enhance the productive capacity of small traditional farmers and fishermen - increase the food production and incomes of poor households, and provide infrastructure, encourage efficient utilization of water in agriculture.. 	<ul style="list-style-type: none"> - Increase Access to Farmland by poor farmers by distributing plots (with Priority to women farmers) - Reorient extension and research system towards addressing priority problems and concerns of subsistence farmers - Support building small dams to harness the seasonal water flows and rehabilitation of degraded catchments - implementing integrated agro - livestock - rangeland support - Supporting the development of smallholder irrigation with high levels of community participation and diversify into higher value crops. - strengthening the cooperatives of artisanal fisheries and improving fisheries infrastructure 	<ul style="list-style-type: none"> - the productive capacity of traditional agriculture and fisheries increased substantially. - Income of farming households and coastal villagers increased from agriculture, livestock and fisheries and the household food security enhanced - employment opportunities of subsistence farmers increased substantially
2. Micro and small enterprises.	Enhance opportunities for job creation and enhancing income	<ul style="list-style-type: none"> - Promoting development of viable small enterprises 	<ul style="list-style-type: none"> - micro enterprises established and operate effectively and profitably providing job opportunities to

	earning opportunities of the poor	<ul style="list-style-type: none"> - improve product quality and design of local micro-industrial products and handicrafts for domestic and external markets. - Increase access to micro credit facilities by the poor 	<ul style="list-style-type: none"> - thousands of workers and the poor - the income earning and employment opportunities of the small enterprises increased
3.Public Works programs	<ul style="list-style-type: none"> - Adopt as essential instruments for employment and income generation for the poor - improve the economic and social conditions of people living in the poorest and drought affected areas - improve people's access to markets and services -promote environmental protection and natural resource conservation 	<ul style="list-style-type: none"> - Finance rehabilitation of social and economic infrastructure through Community Development Fund - Support public works schemes (Cash For Work) in road rehabilitation and maintenance, soil conservation, forestry and water supply and sanitation scheme - strengthen ownership and foster community participation, by requiring contribution of at least 10 percent of the project cost (in kind, cash or labor). 	<ul style="list-style-type: none"> - Increased access to essential basic services built in rural communities and small urban centers - The economic and social conditions of people living in the poorest and drought affected areas of the country improved - Thousands of poor people employed and earned income from the public works schemes

Pillar III: Enhancing Human Resources Development

Area	Objectives	Strategies and Measures	Expected Outcome
1. Education	<ul style="list-style-type: none"> - Increasing access to education at all levels, decrease repetition rate and out rates, especially for girls and disadvantaged children - Improving the quality of basic and secondary education - Developing technical skills and technology training - Strengthening sector capacity to deliver better quality education <u>services</u> 	<ul style="list-style-type: none"> - construction of low cost but durable classroom and ancillary facilities and targeted interventions aimed at girls and other disadvantaged children. - expanding teacher training and professional support, replacement of expatriate teachers by Eritreans at secondary level; development of curriculum and pedagogical reforms. - expanding existing technical schools establishing new ones with due attention to effectiveness and the technical skills and trained geared to meet labor market demand. - developing institutional capacity of the 	<ul style="list-style-type: none"> - Increased literacy rate, lower drop out and repetition rates particularly for girls and disadvantaged children - Primary school enrollment and completion rate increased; - Progress towards meeting the MDGs achieved from an increase in enrollment ratio; Gross Enrollment Ratio (GER) in elementary from 61% to 72%; Middle school from 44% to 45%; High School from 24% to 30%; 30 % GER in tertiary education including technical and vocational training; - adult illiteracy reduced from 70% to 35% - labor market needs satisfied

		<p>Ministry and Zobas in policy planning management and monitoring and evaluation (M&E) to implement a rapid transformation the education sector.</p> <ul style="list-style-type: none"> - Increase Government expenditures on education during 2004 -06 	
2. Health Sector	<ul style="list-style-type: none"> - Improve the health status of the population - Increase access to primary healthcare service and the quality of health 	<ul style="list-style-type: none"> - Primary Health Care Policy (PHCP) continued eliminate the four diseases that pose the most serious public health problems (HIV/AIDs, ma-STD and TB) - develop program in early childhood education and care, improve child and maternal nutrition, strengthen child and maternal health services, improve nutrition education /public awareness - strengthening human and financial capacity in the Zoba and sub-zobas health offices - pay special attention to developing healthcare services to the nomadic population. - increase Government expenditures on public health during 2004 -06 	<ul style="list-style-type: none"> - The incidence and prevalence of these four diseases decreased substantially - public health services (access and quality) improved in both rural and urban areas - achieve infant mortality rate reduced to 40 per 1000 live-births (LB), under five mortality rate reduced to 85 per 1000 LB, child mortality rate reduced to 40 per 1000 LB, deliveries attended by health workers increased from 32 percent to 45 percent.
3. Protecting the vulnerable and Social Safety Net	<p>Meet the basic needs of those who cannot provide for themselves with emphasis on the vulnerable groups including women and children</p> <p>Empower vulnerable and disadvantaged persons, including disabled war veterans, children that are orphans, street children, commercial sex workers and the very poor</p>	<ul style="list-style-type: none"> - Assist socially disadvantaged persons such as the destitute, orphan host families, displaced returnees and deportees, persons with disability and elderly - develop and introduce a sound social security and pension system - empower vulnerable and disadvantaged persons including disabled war veterans, and the very poor 	<ul style="list-style-type: none"> - disadvantaged members of the society by acquiring skills training become productive members of the society - system for the provision of essential food assistance, shelter, medical care, and other basic goods and services to the disabled strengthened - pension scheme made operational by early 2004
4. Women	<ul style="list-style-type: none"> - advance the status of women to actively participate and take a leadership role in national building 	<ul style="list-style-type: none"> - designate focal points in key sector ministries and public agencies to promote gender mainstreaming in the national and sector policies and programs 	<ul style="list-style-type: none"> - Women's skills enhanced; increased opportunities for employment and earning income - programs targeted at the poor and vulnerable groups

	- enhance their economic empowerment, food security and income	- improve social and economic infrastructure Increase their access to farm land and extend loans (or grants) for use in self-help activities	effectively transferred resources, improved family health and nutrition, raised awareness of proper nutrition, childcare, sanitation, and health care; and provided supplementary feeding
5. Affordable Housing	- Improve the quality for the urban poor	- promoting lower cost and affordable housing (technology, materials); - exploring options to use domestically available construction materials in a cost effective manner; - addressing as a matter of urgency the inefficiency in urban land and housing administration; - adopting new and innovative approaches in affordable real estate financing and increasing access to credit - encourage the private sector to engage in the construction of low-cost housing.	- promoting lower cost and affordable housing (technology, materials); - exploring options to use domestically available construction materials in a cost effective manner; - addressing as a matter of urgency the inefficiency in urban land and housing administration; - adopting new and innovative approaches in affordable real estate financing and increasing access to credit - encourage the private sector to engage in the construction of low-cost housing.

Pillar IV: Strengthening Institutional Capacity For Efficient Public Sector Management

Area	Objectives	Strategies and Measures	Expected Outcome
1. Fiscal and financial Management	enhance efficiency and accountability in resource mobilization and allocation	- strengthening institutional capacity - strengthen the existing public expenditure and financial management system that will include an improved public procurement procedure that enhances efficiency and accountability - Instituting a systematic appraisal of large public investment projects before a budget is committed by the government - Continue the zero tolerance policy on corruption - Improve public accounting and auditing - Reform public Enterprises that would not be immediately privatised to operate as	institutional capacity in fiscal and financial management and efficiency and accountability in resource allocation strengthened public enterprises operate as viable and efficient business entities most of the remaining public enterprises privatised

		business enterprises to enhancing their efficiency	
2. Civil service reform	<ul style="list-style-type: none"> - develop a civil service with enhanced profession and dedication to public service. - Establish and implement a sound Pension Scheme, salary reforms and sustainable system of compensation for government civil servants. - improve effectiveness and efficiency in service delivery and public administration 	<ul style="list-style-type: none"> - Conduct short and medium term capacity building and training program to re-equip public servants with the skills essential for efficient and effective service delivery - Formulate and introduce a sound new pension scheme for those currently in the government service and increase pays and benefits of public service personnel - Strengthen the institutional capacity of the civil service and introduce and apply modern management systems. 	<ul style="list-style-type: none"> - Civil service with enhanced professionalism and service oriented established - Sound pension program established and became operational starting May2004 and is effectively managed - The General public and the private sector receive quality and timely services;
c) devolving power to regional administration	<ul style="list-style-type: none"> - develop capacity of institutions at the grass roots level for the provision of social services such as health, education, family planning, sanitation, and clean drinking water 	<ul style="list-style-type: none"> - strengthen capacity of regional governments to deliver services including their finances - strengthen their finances through the implementation of revenue mobilization and financial management capacity - Carry out the decentralization of budget to the Zoba levels. - create support institutions at the regional and district levels to facilitate the overall monitoring and evaluation of PRSP indicators 	<ul style="list-style-type: none"> - Regional governments increasingly take responsibility to deliver services and implement projects using more community based approaches - devolve powers and responsibilities, including those related to social services, from the central to provincial levels to elected district level authorities and local council. - adequate financial and human resources available to the regional administration